United States Court of Appeals

for the

District of Columbia Circuit

TRANSCRIPT OF RECORD

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REPLY BRIEF FOR PETITIONERS

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 20,889 - 20,894

JOHN H. VERKOUTEREN, ET AL.,

Petitioners,

v.

DISTRICT OF COLUMBIA,

Respondent.

Petition for Review of a Decision of the
District of Columbia Tax Court

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REPLY BRIEF FOR PETITIONERS

I

In this case, the parties agree that immediately prior to its liquidation on January 29, 1960, Capitol Hotel Enterprises, Inc. ("Capitol"), had earned surplus of $99,821.30. The parties are also in agreement that the liquidation of Capitol and the distribution of its assets, including the Chastleton Stock, to its shareholders produced the following consequences under the District of Columbia Income and Franchise Tax Act:

(1) First, Capitol's shareholders, as a result of the liquidation, received, and were required to report, a

dividend equal to the amount of Capitol's earned surplus immediately prior to the liquidation ($99,821.30). Berliner v. District of Columbia, 103 App. D.C. 351, 258 F. 2d 651 (1958), cert. denied, 357 U.S. 937 (1958).

(2) Second, Capitol's distribution to its shareholders of the Chastleton Stock did not result in a realization by Capitol of taxable income to the extent that the fair market value of the Chastleton Stock ($390,000) exceeded Capitol's cost basis ($20,480). District of Columbia v. Oppenheimer, 112 App. D.C. 239, 301 F. 2d 563 (1962) [This case is hereinafter referred to as the "first Oppenheimer case."]

(3) Since the unrealized appreciation in value of the Chastleton Stock held by Capitol was not realized by Capitol as a result of the liquidating distribution of the Chastleton Stock to its shareholders, the unrealized appreciation in value did not increase Capitol's earned surplus above $99,821.30 and was not taxable to Capitol's shareholders as a dividend. First Oppenheimer case, supra.

Up to this point, the Petitioners and the District appear to be in complete agreement on the tax consequences of Capitol's liquidation. The District, however, concludes (Brief for Respondent, p. 5) that the basis for the Chastleton Stock in the hands of the Petitioners, who were the shareholders of Capitol, must be the "amount of the liquidating 'dividend'

represented in the value of the assets received," or the amount of Capitol's earned surplus of $99,821.30. There is no provision of the District of Columbia Income and Franchise Tax Act nor any decision of this Court supporting the District's argument, and none is cited by the District in its brief.

The District relies on the Tax Court's decision in Oppenheimer v. District of Columbia, Opinion No. 1029, 92 W.L.R. 799 (May 8, 1964), affirmed, 124 App. D.C. 221, 363 F. 2d 708 (1966) [hereinafter referred to as the "second Oppenheimer case"], holding that the basis of assets distributed in a corporate liquidation was equal to the distributing corporation's earned surplus plus the shareholder's original capital investment. We submit, however, that the Tax Court's decision in the second Oppenheimer case will not withstand a reasoned analysis and is clearly erroneous.

First, the Tax Court allowed itself to be mislead by assuming that there was a fixed relationship between the amount of the liquidating distribution taxed to the shareholders as a dividend and the shareholders' basis for the distributed property, and by ignoring the clear, overriding policy of the District of Columbia Income and Franchise Tax Act exempting capital gains from tax. In other words, the Tax Court assumed that since the appreciation in value of the corporate assets was not realized by the corporation -- and was not taxed to its shareholders as a dividend -- in connection with the corporation's liquidation, such unrealized value could

not be included in the shareholders' basis for the property after the liquidation.

The basis problem involved in the second Oppenheimer case -- and in this case -- is not, as the Tax Court assumed, co-extensive with the dividend question involved in the first Oppenheimer case. In the first Oppenheimer case, this Court held that the unrealized appreciation in value of a corporation's assets was not realized by the corporation when it made a liquidating distribution to its shareholders. Since the unrealized appreciation was not realized by the corporation, it could not be included as a part of the corporation's earned surplus and could not be taxed to the shareholders as a dividend under D. C. Code § 47-1551c(m).

The first Oppenheimer case does not stand for the proposition that this appreciation in value is not realized by the shareholders upon their receipt of the liquidating distribution. On the contrary, it is a basic principle of income taxation that in a corporate liquidation a shareholder does realize income measured by the excess of the fair market value of the property received over his cost basis for his stock. Treas. Regs. 1.331-1(b); Treas. Regs. 1.1001-(a); Bittker and Eustice, FEDERAL INCOME TAXATION OF CORPORATIONS AND SHAREHOLDERS (2d ed., 1966), Sec. 9.01 et. seq. Such income is realized not as a dividend, but as gross income "derived from any source whatever." D. C. Code 47-1557a(a). Realization of income by the shareholder is a necessary corollary of the historic treatment of a corporation and its shareholders

as separate and distinct taxable entities. Moline Properties, Inc. v. Commissioner, 319 U.S. 436 (1943).

As we pointed out at considerable length in our main brief (Brief for Petitioners, pp. 17-25), under the District of Columbia Income and Franchise Tax Act, a liquidation is, in part, an "exchange," and the shareholders' gain on liquidation -- to the extent attributable to unrealized appreciation in value of corporate assets -- is not subject to tax. Although the gain represented by the unrealized appreciation in value of the distributed property is not realized at the corporate level, it is realized at the shareholder level. However, this gain is a capital gain and is exempt from tax at the shareholder level, except for the amount otherwise taxable as a dividend under this Court's decision in the Berliner case. Thus, although the tax at the shareholder level is measured by the amount of the distribution treated as a dividend -- i.e., the corporation's earned surplus -- the shareholders' cost basis for the distributed property must necessarily reflect the greater fair market value of the distributed property. If the shareholders' basis does not include the full fair market value of the distributed property, a later sale of the property would subject the shareholders to a tax on the gain which the District of Columbia Income and Franchise Tax Act declares is exempt from tax.*

* In its opinion in the second Oppenheimer case, the Tax Court observed that "[i]t is a cardinal principle in the logic or science of taxation that a stepped-up or change of basis is not permissible in cases of a non-taxable transfer." Likewise, the District in its brief (Brief for [Footnote continued on next page]

Second, the Tax Court's reliance on D. C. Code § 47-1583c is also misplaced. That section provides that the basis of property other than money "paid as a dividend" shall be fair market value. This section by its very terms applies only to property "paid as a dividend." It can have no application to that portion of a liquidating distribution which, under this Court's decision in the first Oppenheimer case, is not a "dividend." It seems obvious that D. C. Code § 47-1583c was intended to apply to ordinary dividends in kind, not to the non-dividend portion of a liquidating distribution.

On first blush, it may seem to have been an oversight on the part of the draftsmen of the District of Columbia Income and Franchise Tax Act in not specifically spelling out the basis for property distributed as a liquidating distribution. This was not, however, the case. The drafts-men obviously thought there was no necessity to include the non-dividend portion of a liquidating distribution within the ambit of D. C. Code § 47-1583c -- nor any other provision -- because of the belief that the basis of the non-dividend portion of the liquidating distribution was

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[Footnote continued from preceding page]
Respondent, p. 9) quotes Mertens for the same proposition. We may assume that this is a fair statement of the general policy of the Federal income tax laws, where the concept of a "non-taxable transfer" is predicated on a transaction in which realized gain is not recognized (i. e., the gain is deferred) and a transferred or substituted basis is used to insure that the deferred gain will ultimately be subject to tax. Both the Tax Court and the District fail to appreciate that the concept of a non-recognized gain is a term of art under Federal tax law which is not synonymous with exempt gain, and that the overriding policy of the District of Columbia Income and Franchise Tax Act exempting capital gains from tax -- a policy not contained in Federal law -- requires a departure from the principles of the Federal law.

adequately covered by D. C. Code § 47-1583, which provides that the basis of property shall be its "cost." It is significant to note that this gap in the statute was present in the Internal Revenue Code of 1939, upon which the District of Columbia Income and Franchise Tax Act was patterned, where the draftsmen also failed to include a basis provision specifically applicable to property received pursuant to a corporate liquidation. But, notwithstanding the absence of specific statutory authority, the general cost basis provision of the 1939 Code was held to be applicable in determining the basis of property received on liquidation. S. Rep. No. 1622, 83rd Cong., 2d Sess. 256 (3 U.S.C. Code Cong. & Adm. News 4894 (1954)); Bittker and Eustice, _supra_, Sec. 9.04.

Although this Court affirmed the result reached by the Tax Court in the second _Oppenheimer_ case, it did so without expressly deciding what Mrs. Oppenheimer's basis was for the property she received as a liquidating distribution. Even though this Court did hold in the second _Oppenheimer_ case that Mrs. Oppenheimer's basis was not fair market value, we believe that a different conclusion would have been reached in that case if the Court's attention had been directed to the relationship between the question of basis and the overriding policy of capital gains exemption.

Without unnecessarily prolonging our discussion of this aspect of the District's brief, we believe that three other arguments made by the District in its brief deserve comment:

1. Contrary to the District's contention (Brief for Respondent, pp. 9-10), the Petitioners' argument in this case cannot be equated with the District's unsuccessful argument in the first Oppenheimer case. In the first Oppenheimer case, the District argued that the appreciation in value of the liquidated corporation's assets was realized by the corporation when it distributed its assets in liquidation and that this realized value increased the amount of the dividend taxable to the shareholders. The first Oppenheimer case did not involve any argument by the District that the shareholders of the liquidated corporation realized income on the liquidation -- to the extent the fair market value of the distributed assets exceeded their cost basis for the stock -- under the general provisions of D. C. Code § 47-1557a(a). Undoubtedly the reason this argument was not made was because the District recognized, and apparently still recognizes, that such income was an exempt capital gain. In fact, in the first Oppenheimer case one of the arguments made by the District to this Court in order to convince this Court to accept the District's "dividend" argument was that the shareholders would get a fair market value basis for the distributed assets without paying tax on the appreciation in value. See Brief for Petitioner, Docket No. 16,472, p. 10. Petitioners' argument in this case is, therefore, wholly consistent with this Court's decision in the first Oppenheimer case. It is the District which is now taking an inconsistent position.

2. Contrary to the District's contention (Brief for Respondent,

p. 10), the Petitioners' argument, that the portion of the liquidating distribution in excess of Capitol's earned surplus was received in exchange for the underlying stock, is in no way comparable to the facts involved in the Berliner case. As we have noted in our Brief (Brief for Petitioners, p. 18), and as Judge Prettyman recognized in his opinion in Snow v. District of Columbia, 124 App. D.C. 69, 71, 361 F. 2d 523, 524-525 (1965), Berliner dealt exclusively with "a distribution of earnings, an earned surplus." The present cases are entirely distinguishable from Berliner because in Berliner the corporation had sold all of its assets to a third party prior to liquidation, had realized the entire amount of the appreciation in value inherent in its assets, and this appreciation in value had been converted into realized income, that is, earned surplus, at the corporate level which, when the corporation was liquidated, was taxable to its shareholders as a dividend. Unlike the corporation involved in the Berliner case, Capitol did not sell its assets to a third party prior to liquidation and did not convert the unrealized appreciation in the value of its assets into a realized earned surplus. We submit that the absence of a realization of income at the corporate level serves completely to distinguish the Berliner case from the present cases.

3. The District's attempt to distinguish the Snow case (Brief for Respondent, pp. 11-12) may readily be dismissed with the simple observation that this Court, in Snow, (124 App. D.C. 69, 73, 361 F. 2d 523, 527) held that Mr. Snow's cost basis for the assets distributed by

Lombardy, Inc., was equal to his cost "which is the value of the stock he turned over for the property."

II

Part II of the Petitioners' brief (Brief for Petitioners, pp. 31-40), and the corresponding portion of the District's brief (Brief for Respondent, pp. 13-19), deal with the Petitioners' alternative argument that they are entitled to add to their holding period for the Chastleton Stock received by them upon the liquidation of Capitol either (1) the 12-year period in which Capital held the Chastleton Stock, or (2) the 12-year period in which Petitioners held their capital stock in Capitol. If either of these time periods may be "tacked" to Petitioners' holding period for the Chastleton Stock, then the Chastleton Stock constituted a capital asset in Petitioners' hands and the gain realized by them upon the later sale was an exempt capital gain. Petitioners, in their principal brief, have advanced a number of arguments in support of their position that "tacking", even though not expressly permitted by the literal language of the District of Columbia Income and Franchise Tax Act, is nevertheless a part of that law as a fundamental principle in the common law of income taxation. We do not believe that the District has advanced any reason why this Court should not hold that "tacking" is permitted under the District of Columbia Income and Franchise Tax Act on the facts of these cases.

First, the District challenges the applicability of Section 1223(2) of the Internal Revenue Code of 1954 because of its belief that Section 1223(2) is in some way dependent upon the existence of a sale or exchange. Section 1223(2) is a codification in the Federal income tax law of the general principle of "tacking" sanctioned by early administrative interpretations of the Federal law which were made in the absence of express statutory authorization. (Brief for Petitioners, p. 36). It is clear from the language of Section 1223(2) that it does not depend for its application upon the existence of a sale or exchange. Thus, the text of the statute itself states in its preamble that it applies to "property however acquired." In other words, Section 1223(2) provides that in determining a taxpayer's holding period for property <u>however acquired</u>, the holding period of another person shall be included if that property has a basis in the hands of the taxpayer for determining gain or loss from a sale or exchange which is the same in whole or in part as the basis for the property in the hands of the person from whom it was acquired. The sale or exchange referred to is not the transaction by which the property was acquired, but is a reference to a subsequent transaction in which the property is disposed of and for which it is necessary, in characterizing the nature of the gain or loss from such subsequent transaction, to determine the holding period for the property.

Second, the District's attempt to distinguish the case of <u>District of Columbia</u> v. <u>Lewis</u>, 109 App. D.C. 353, 288 F. 2d 137 (1961), seems

to us also to be erroneous. In Lewis, the question was whether a transfer from a husband to his wife in lieu of his obligation of support was made for "full consideration in money or money's worth" within the meaning of D. C. Code § 47-1601(a). The meaning of the quoted language for D. C. tax purposes had never been construed by the courts, but the identical phrase had been included in the Federal income tax law for many years. Moreover, a specific provision of the Internal Revenue Code (Section 2043(b) of the Internal Revenue Code of 1954) specified certain types of consideration which, for purposes of Federal law, were not to be considered equivalent to a "consideration in money or money's worth." One of the types of consideration which the Federal statute expressly stated was not to be considered a "consideration in money or money's worth" was a relinquishment of "other marital rights." In holding that a transfer by a husband to his wife in lieu of the husband's obligation of support was not a relinquishment of "other marital rights," and therefore was made for "full consideration in money or money's worth," this Court clearly treated the matter as if the provision of Federal law -- namely, that a relinquishment of "other marital rights" was not a "consideration in money or money's worth" -- was expressly made a part of the D. C. Code. This is clear from the statement in this Court's opinion in the Lewis case that "the problem of the instant case, then, lies in determining whether a wife's right to support is one of the 'other marital rights' referred to in the sections quoted above." 109 App. D.C. 353, 356, 288

F. 2d 137, 140. If this Court did not intend to treat the provision of Federal law as if it has been incorporated in the D. C. Code, there would have been no need to demonstrate that support was not one of the "other marital rights."

Just as the provision of the D. C. Code involved in the Lewis case did not define the phrase "consideration in money or money's worth," the statutory provision involved in these cases -- D. C. Code § 47-1557c(1) -- does not define the phrase "held by the taxpayer." However, for many years the principle of "tacking" reflected in Section 1223(2) of the 1954 Code has been applied, with and without the benefit of express statutory authorization, in determining the holding period of property for purposes of applying the capital gain and loss provisions of Federal law.

Finally, the District has failed to advance any cogent reason why the decision in Helvering v. New York Trust Company, 292 U.S. 455 (1934), which held that "tacking" was a part of Federal tax law independent of any express statutory authorization, is inapplicable to the present cases. To say, as the District has said, that the principle of the New York Trust Company case should not be applied because it involved a trust, while these cases involve a corporate liquidation, ignores the thrust of Petitioners' argument and would unnecessarily limit the decision without justification. The New York Trust Company case establishes the principle that "tacking" may exist despite the absence of a statute, because, in the words of the Supreme Court (292 U.S. 455, 467), "No valid ground has been suggested

for requiring tenures to be added for one purpose [i. e., in determining basis] and forbidding the combination for the other [i. e., in determining holding period]." Indeed, while it is true that there is nothing in the Supreme Court's opinion to indicate that the rule applied to trusts would also be applied to corporate liquidations, it would seem to us to be of even greater significance that there is nothing in the opinion to indicate that a different rule would be applied in one case than in the other.

Respectfully submitted,

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IN THE UNITED STATES COURT OF APPEALS

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NOS. 20,889 - 20,890 - 20,891
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John H. Verkouteren, et. al.,
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On Review of a Decision of
the District of Columbia Tax Court, En Banc

BRIEF FOR WATERGATE REALTY, INC., AMICUS CURIAE

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BRIEF FOR WATERGATE REALTY, INC., AMICUS CURIAE

QUESTION PRESENTED

Whether the three-judge panel erred in deciding that, for purposes of the District of Columbia Income and Franchise Tax Act, (1) the basis of property distributed to shareholders in a corporate liquidation is its cost to the liquidated corporation and (2) the holding period of such property to the shareholders who receive it begins on the date of such liquidation, and does not include the period during which the property is held by the corporation.

INTEREST OF AMICUS CURIAE

Watergate Realty, Inc. ("Realty"), a District of Columbia corporation, is currently engaged in administrative proceedings with the tax officials of the District of Columbia with regard to the basis and holding period, in its hands, of property received in liquidation of a wholly owned subsidiary and subsequently sold by it. Since the case at bar will have a significant bearing on Realty's position in the pending matter, Realty respectfully submits this brief, *amicus curiae*, to bring its views with respect to the applicable District of Columbia law to the attention of this Court.

STATEMENT OF THE CASE

Capitol Hotel Enterprises, Inc. (Capitol), a District of Columbia corporation, was liquidated in 1960, distributing to its shareholders (including petitioners who held sixty percent of Capitol's stock), among other assets,* Chastleton Hotel, Inc. (Chastleton) stock. Capitol had acquired the Chastleton shares in 1948 at a cost of $20,480. Three days later, petitioners sold the Chastleton stock thus received for $234,000.

On their District of Columbia income tax return for the year 1960, petitioners, all individual residents of the District filing on a cash basis, did not report any taxable income attributable to the receipt or sale of the Capitol stock.

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*The other assets consisted of notes receivable and accrued interest having a book value of $80,541.30. At liquidation, Capitol had earned surplus of $99,821.30.

The D. C. tax authorities subsequently determined: (1) that the property distributed in liquidation was taxable as a dividend to the extent of Capitol's earned surplus, and (2) that the gain ($234.000 less petitioners' basis of $12,288*) realized on the sale of Chastleton shares was taxable. Petitioners acceded to the assessor's determination with respect to dividend taxation, but challenged this treatment of the Chastleton stock sale. They brought suit in the District of Columbia Tax Court to recover that portion of the deficiency assessed and paid.

This case twice has been considered by the D.C. Tax Court and by this Court. The Tax Court originally sustained the assessment on the ground that the stock had been sold by the corporation, rather than the shareholders. Petitioners appealed. This Court reversed the Tax Court's finding as to sale by the corporation and remanded the case for further consideration. Verkouteren v. District of Columbia, 120 U.S. App. D.C. 361, 346 F.2d 842 (1965). The Tax Court again upheld the assessment. On appeal, the three-judge panel affirmed, holding: (1) that the basis of the Chastleton stock in petitioners' hands is its cost to Capitol, but (2) that the gain realized upon the subsequent sale is taxable because such stock was not held by the shareholders for more than two years and, consequently, was not a capital asset.

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*Petitioners' basis was computed at sixty percent of $20,480, the basis in Capitol's hands of the Chastleton stock.

Petitioners moved for a rehearing before the three-judge panel or _en banc_. On April 8, 1969, this Court, _en banc_, vacated the opinion and judgment filed by the three-judge panel on February 6, 1969, and directed a rehearing by the entire Court.

SUMMARY OF ARGUMENT

The question to be decided in this case is the basis and holding period, for purposes of the District of Columbia income tax law, of property received by a shareholder (other than out of earnings and profits) in liquidation of a corporation. The three-judge panel held that the basis of such property to the shareholder-recipient is its cost to the liquidated corporation, but that the shareholder's holding period begins with the date of distribution. _Amicus curiae_ respectfully submits that the panel's determination of basis was correct, but that the Court erred in refusing to find that the shareholder's holding period runs from the corporation's acquisition of the property. Under fundamental principles of tax law, as applied by the United States Supreme Court, a taxpayer inheriting another's basis inherits his holding period as well.

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ARGUMENT

THE BASIS OF PROPERTY DISTRIBUTED TO A SHAREHOLDER IN LIQUIDATION IS ITS COST TO THE LIQUIDATING CORPORATION, AND THE HOLDING PERIOD OF SUCH PROPERTY BEGINS WITH ITS ACQUISITION BY THE CORPORATION

Under the District of Columbia Income and Franchise Tax Act, corporate distributions out of earnings and profits, whenever made, constitute taxable dividends. D. C. Code §47-1551c. Accordingly, that portion of a liquidating distribution which is covered by corporate earnings and profits is taxed as a dividend, notwithstanding the fact that the taxpayer surrenders his stock to the corporation. Berliner v. District of Columbia, 103 U.S. App. D.C. 351, 258 F.2d 651 (1958), cert. denied, 357 U.S. 937 (1958). The question before this Court is the basis and holding period of property received in a liquidating distribution not out of earnings and profits.*

Amicus curiae respectfully submits:

(1) that the basis of property distributed in a corporate liquidation is determined by reference to the corporation's cost, since a corporate liquidation is a non-taxable event, and not a sale or exchange; and

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*All references to corporate liquidations hereafter made assume an absence of earned surplus, since taxation of distributions to the extent thereof is not in dispute.

(2) that for the purpose of determining whether such property is a capital asset, the corporation's holding period is tacked onto the shareholders' holding period.

I. <u>The Basis Of Property Distributed To A Shareholder Is Its Cost To The Liquidating Corporation, Because A Corporate Liquidation Is Not A Sale Or Exchange.</u>

Pursuant to D.C. Code, Section 47-1583, "[T]he basis for determining the gain or loss from the sale, exchange, or other disposition of property shall be the <u>cost</u> of such property." (Emphasis added.) The fair market value of petitioners' stock at the time of liquidation could constitute such a "cost" for the distributed property only if the liquidation constitutes an exchange between the corporation and its shareholders.

In the case at bar, petitioners contended that the Capitol liquidation was an exchange of Capitol for Chastleton stock, resulting in a basis for the Chastleton stock equal to its fair market value. Since the Capitol stock was a capital asset, having been held for more than two years, this theory results in no gain being realized on the liquidation exchange.

The panel correctly rejected petitioners' argument. Pointing out that "the capital gain exclusion is limited to transactions involving a 'sale or exchange' of a capital asset," it held "that distributions to stockholders from the corporation's capital, although accompanied by extinction of all outstanding stock in the corporation, are neither sales nor exchanges." <u>Verkouteren</u> v. <u>District of Columbia</u>, _______ U.S. App. D.C. _______, _______ F.2d _______ (Feb. 6, 1969,

Slip.Op. pp. 9-10). Accordingly, the court determined that the basis of the Chastleton shares in the shareholders' hands was not its fair market value at the time of distribution, but rather $20,480, the cost of the stock to the corporation.

A. The Precedents Under The District of Columbia's Income Tax Law

With one aberration to be discussed below, the panel's decision in this case with respect to the nature of a corporate liquidation and the basis of property received thereby accords fully with the decisions of this Court.

The leading case prior to the panel's decision is Oppenheimer v. District of Columbia ("Oppenheimer II"), 124 U.S. App. D. C. 221, 363 F. 2d 708 (1966). In that case, this Court decisively rejected the argument that a corporate liquidation constitutes an exchange between a corporation and its shareholders. The issue in Oppenheimer II was the basis for depreciation of property (real estate) received by a taxpayer as a liquidating distribution. The Court previously had held that unrealized appreciation in the value of such real estate was not included in determining the liquidated corporation's earned surplus and, therefore, was not subject to taxation as a dividend. Oppenheimer v. District of Columbia (Oppenheimer I), 112 U.S. App. D.C. 239, 301 F. 2d 563 (1962). Relying upon D.C. Code §47-1583 (b), which provides that the depreciation basis of assets received in exchange for other property "shall be the market value thereof at the time of such exchange," the taxpayer contended:

(1) that the property in question had been acquired in exchange for her stock in the liquidating corporation, and (2) that she was therefore entitled to a depreciation basis reflecting the unrealized and untaxed (Oppenheimer I) appreciation in the value of the asset.

This Court faced and denied the taxpayer's exchange argument. As Judge McGowan explained (Oppenheimer II, 124 U.S. App. D.C. at 224):

> "In classic corporate theory, however, uncomplicated by tax considerations, the liquidating distribution by a dissolved corporation of its assets to its shareholders does not partake of the nature of a bargained sale or exchange. One of the rights of a stockholder is to share in the distribution of the assets of a corporation as and when it goes out of existence. His shares are turned in for extinction, and he takes as of right his proportion of the assets formerly owned by the corporation. See First National Bank of Boston v. State of Maine, 284 U.S. 312, 330, 52 S. Ct. 174, 76 L.Ed. 313 (1932)."

Turning to the provisions of the D.C. Code, the Court reaffirmed its decision in Berliner v. District of Columbia, supra, that a corporate liquidation is not an exchange under the District's tax law, as follows (Oppenheimer II, 124 U.S. App. D.C. at 224):

> "In Berliner, supra, it was argued to this Court that a distribution in corporate liquidation should not be included in taxable income because it represented 'gains from the sale or exchange of [a] capital asset' within the meaning of Section 1551c(l), and was therefore exempt from taxation by reason of Section 1557a(b) (11). We rejected that contention, noting that, at least for purposes of inclusion in taxable income, Congress had, in Section 1551c(m), made express provision for distributions in corporate liquidation. Although Congress has, to put it mildly, been appreciably

> less precise in addressing itself to the depreciation basis of property received in liquidation, we do not think that we are forced to fix such basis [for depreciation] by reference to the 'exchange' category set forth in Section 1583e. To do so would be to say that a stockholder, simply by deciding to dissolve and liquidate the corporation, may acquire a depreciation base consisting of a book write-up of a value on which, very properly, no tax need be paid upon its receipt by the stockholder. We think it much more likely that Congress intended to have its express -- and only -- language in the District taxing statute point the way for handling the depreciation basis of property distributed in liquidation."

The Court found further support for its treatment of corporate distributions in the comparable provisions of the Internal Revenue Code, pointing out that (*Ibid*.):

> "When Congress addressed itself to the problem of fitting corporation liquidations into its scheme of capital gains taxation for federal taxpayers generally, it thought it necessary to say that distributions in liquidation '*shall be treated as* payments in exchange for stock or shares . . .' (Emphasis supplied). In the income tax statute made applicable to the District of Columbia -- so vastly different as it is in its approach to capital gains taxation -- Congress has made no similar provision. We are, thus, under no compulsion to hold that a transaction which Congress has found it necessary to say 'shall be treated as' an exchange in one context must be taken to be one in another."

Oppenheimer II thus is controlling authority for the proposition that a corporate liquidation does not involve an exchange. The same result was reached in *Dupont Park Apartments, Inc.* v. *District of Columbia*, 120 U.S. App. D.C. 215, 345 F. 2d 109 (1965).

The question presented in that case was the deed recordation tax payable with respect to the conveyance of property from a liquidating corporation to trustees for the stockholders. Pursuant to D. C. Code §45-723, the recordation tax is based upon "the consideration for such deed." However, "[W]here no price or amount is paid or required to be paid, . . . the consideration for the deed to such property shall . . . be construed to be the fair market value of the real property, and the tax shall be based upon such fair market value." D.C. Code §45-724. The D.C. Tax Court held that the stockholders, in consideration of the distribution, paid $207,335.03, the Corporation's net earned surplus. The recordation tax accordingly was based on that amount.

Reversing the Tax Court, the Court of Appeals held that " 'no price or amount' was 'paid or required to be paid' for the deed." Dupont Park Apartments, Inc. v. District of Columbia, 120 U.S. App. D.C. at 216. Accordingly, the Court concluded that (Ibid.):

> "The recordation tax must therefore be based upon the fair market value of the property [$1,900,000]. We cannot accept the District of Columbia Tax Court's conclusion that, by giving up their equity in what the court described as the 'realized value' of the real property, $207,335.03, which appeared on the corporation's balance sheets as earned surplus, the stockholders paid the amount for the deed." [Emphasis added.]

By rejecting the contention that the stockholders gave consideration for property received as a liquidating distribution, the Court of Appeals in the Dupont Park Apartments squarely held that such a transaction is not an exchange.

District of Columbia v. Goldman, 117 U.S. App. D.C. 219, 328 F.2d 520 (1964), is not inconsistent with this view. The issue in that case concerned taxation of distributions, not out of earnings and profits and not in liquidation, from a corporate depreciation reserve. The Court of Appeals held that such distributions are not gross income within the meaning of D.C. Code §47-1551a, and thus are not subject to taxation. Significantly, the Court did not analyze the transaction as an exchange between the corporation and its shareholders, did not indicate that the basis of the underlying stock was to be adjusted to reflect the amount of such distribution, did not suggest that the tax consequences would vary depending on the basis of such stock, and did not find that the item would be subject to taxation had such stock been held for less than two years.* The Federal tax cases cited by the Court do hold that depreciation reserve distributions in excess of basis are taxable as capital gains, but the Internal Revenue Code dealt with there, unlike the District of Columbia Income and Franchise Tax Act involved here, expressly so requires. District of Columbia v. Goldman, 117 U.S. App. D.C. at 222, f.n.8, see, Opinion of Washington, J., dissenting, Id. at 224. Accordingly, Goldman must be read as holding only

*Such a finding would result in shareholders being taxed differently on the same distribution, depending on the length of their shareholding. As this Court pointed out in Berliner v. District of Columbia, 103 U.S. App. D.C. at 355, with respect to earned surplus, "Such a difference in treatment for the same distribution would hardly be justified by logic -- and, as we read the statute, Congress has not authorized it."

that such distributions are not gross income.*

Similarly, the D.C. Tax Court, in a number of decisions, has resisted the insistent attempts of taxpayers to treat corporate distributions as exchanges for tax purposes. See, McChesney v. District of Columbia, D.C. Tax Court, Opinion No. 997, D.C. Tax Reporter, CCH ¶200-012 (1962). (Cash received in partial liquidation - disproportionate redemption - held taxable as a dividend to the extent of earned surplus.); Estate of Uline v. District of Columbia, D.C. Tax Court, Opinion No. 1018, D.C. Tax Reporter, CCH ¶200-032 (1962), aff'd. 124 U.S. App. D.C. 5, 360 F.2d 820 (1966) ("The difficulty with such argument or contention [that property received in a liquidating distribution acquires a stepped-up basis] is that the law does not so provide. Section 47-1583(c) relates solely to the sale, exchange or other disposition of assets, which the Court of Appeals said in the Berliner case does not occur when a corporation is dissolved and its assets are distributed to the shareholders."); Goldstein v. District of Columbia, D.C. Tax Court, Opinion No. 1020, D.C. Tax Reporter, CCH ¶200-035 (1963), aff'd. sub nom., Bord v. District of Columbia, 120 U.S. App. D.C. 363, 344 F.2d 560 (1965) ("Under the District of Columbia law the distribution of assets of a dissolved corporation to its shareholders is not a 'sale, exchange or other disposition' of their intangible property, namely, the stock in the corporation.")

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*For the reasons discussed in the text, amicus curiae respectfully submits that Judge Leventhal's contrary construction of the Goldman case in his dissenting opinion in Verkouteren v. District of Columbia, ______U.S. App.______,______F.2d_____(February 6, 1969, Slip. Op. pp. 20-22) is in error.

The only departure from this long-established and otherwise consistent treatment of liquidating distributions is the decision of the Court of Appeals in Snow v. District of Columbia, 124 U.S. App. D.C. 69, 361 F.2d 523 (1965). In that case, the taxpayer had purchased for $1,000,000 all of the stock of a corporation having miscellaneous assets worth $1,000,000 and immediately thereafter liquidated the corporation. As a consequence of the foregoing transactions, the Court held: (1) that the taxpayer received a dividend of $300,000, the amount of the corporation's earnings and profits, (2) that he was entitled to a deductible loss of $300,000 on the theory that he had given up stock having a basis of $1,000,000 in exchange for assets valued at $700,000, deducting the amount taxed as a dividend, and (3) that the distributed property receives a depreciation basis equal to its fair market value. Although the treatment of gain derived from a corporate liquidation was not before the Court in Snow, the rationale underpinning the decision logically requires taxation where the underlying stock was held for a period of less than two years. It follows from Snow similarly that the basis for determining gain or loss in the event of a subsequent disposition of such assets is fair market value..

Snow and Oppenheimer II may be reconciled in result, although not in reasoning. As Judge Fahy pointed out in his dissenting opinion, joined by Chief Judge Bazelon, to the denial of a petition for rehearing en banc in Snow (124 U.S. App. D.C. at 74):

". . . I have substantial doubt about the correctness of the court's decision. There is weighty authority for the view that the transaction described in the opinion should be construed as a payment by petitioner of $1,000,000 not for stock of a corporation with $1,000,000 of assets but for acquisition of assets of the value of $1,000,000, namely, the cash of $300,000 and the apartment house worth $700,000. Thus viewed, the transaction was not in reality an investment in stock but the purchase of property." [Footnote omitted.]

This approach is founded upon the well-established Kimbell-Diamond rule.* As the Court explained in United States v. Mattison, 273 F.2d 13, 17 (9th Cir. 1959), the Kimbell-Diamond rule operates as follows:

". . . when a taxpayer who is interested primarily in a corporation's assets first purchases the stock and then liquidates the corporation in order to acquire the desired assets, the separate steps taken to accomplish the primary objective will be treated as a single transaction. Thus, even though the objective was accomplished in form by a purchase of stock, the substance of the transaction is the purchase of property."

Accordingly, the taxpayer takes as his basis for the assets received on liquidation of the acquired corporation, the price paid for that corporation's stock.

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*Kimbell-Diamond Milling Co., 14 T.C. 74 (1950), aff'd. per curiam, 187 F.2d 718 (5th Cir. 1951), cert. denied, 342 U.S. 827 (1951).

Adopted before the Internal Revenue Code provided a statutory basis for treating a purchase of stock as an asset acquisition*, the Kimbell-Diamond doctrine appears particularly applicable to the facts before the Court in Snow, since the purchase of stock and liquidation of the corporation virtually were accomplished simultaneously. Applying this rule to Snow, the inconsistency with Oppenheimer II and its predecessors is eliminated. Under such approach, there would have been neither a dividend received by, nor a loss allowed to the taxpayer in Snow. The taxpayer would have, as his basis for the property received in liquidation, its purchase price for the stock of the liquidated corporation. Accordingly, the Kimbell-Diamond tax result is identical to that actually reached in the case. But the reasoning in Snow, diametrically opposed to all of the previous and subsequent decisions of this Court, must be regarded as having been effectively overruled by Oppenheimer II.

To summarize, it is clear under District law: (1) that a liquidating distribution is taxed only to the extent of earnings and profits of the dissolved corporation; (2) that neither gain nor loss is recognized thereby; and (3) that the basis for depreciation and determining gain on a subsequent sale or exchange of property received as a liquidating distribution is the property's cost to the liquidated corporation, not its fair market value.

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*The rule subsequently was codified as §334(b) (2) of the Internal Revenue Code.

B. Federal Tax Law Analogy

As this Court pointed out in Oppenheimer II, 124 U.S. App. D.C. at 224, "When Congress addressed itself to the problem of fitting corporate liquidations into its scheme of capital gains taxation for federal taxpayers generally, it thought it necessary to say that distribution in liquidation 'shall be treated as payments in exchange for stock or shares. . .'" (Emphasis in text.) Accordingly, the Court concluded that the treatment of corporate liquidations under the Internal Revenue Code (IRC) offers little guidance for the construction of the very different District of Columbia Income and Franchise Tax Act. Ibid.

Further ground for not incorporating into the District of Columbia tax law the IRC sections (notably Section 331) which provide for exchange taxation of corporate liquidations is afforded by the fact that the Federal statute does not consistently so characterize such transactions.

Thus, where the shareholder is a corporation receiving a liquidating distribution from its subsidiary, the liquidation is a non-taxable event. Section 332(a), IRC. Where the liquidation takes place within one month, there is no tax to the shareholder (whether individual or corporate) unless the corporation has earnings and profits, or stock, securities or money. Section 333(a), IRC. And even where the exchange rules apply, taxation of gain occurs only at the shareholder level; the corporation is not so taxed.

If there is any lesson to be learned from federal taxation of a liquidating distribution, it is that a liquidation may or may not be taxed, but there is never a step-up of basis to fair market value unless a tax is imposed. Under Section 331, the basis of the property received is increased to its fair market value by the operation of Section 334(a), IRC, but only if the distribution is taxed. Should the liquidation escape tax by reason of Section 332, the basis of the property distributed remains unchanged. Section 334(b) (1). In a Section 333 liquidation, the basis of distributed property is increased, but only to the extent that gain is recognized. Section 334(c). The same rule is followed in other sections of the IRC. For example, where a corporation acquires property in a tax-free reorganization, the basis is increased only by the amount of gain recognized. Section 362(b), IRC.

In short, there is nothing in the Federal Tax Law which would support the result for which the petitioners in this case are contending: that property distributed in a tax-free corporate liquidation receives a stepped-up basis.

II. Where a Taxpayer Acquires Property Whose Basis Is the Same As His Transferors, The Taxpayer "Tacks On" His Transferor's Holding Period.

Despite its holding that the basis of the Chastleton stock in the hands of the shareholders is the same as in the hands of Capitol, the three-judge panel refused to credit petitioners with the corporation's holding period for purposes of determining whether the stock was a capital asset when subsequently sold. *Amicus curiae* respectfully submits that this ruling is erroneous, as a matter of law.

Helvering v. New York Trust Co., 292 U.S. 445 (1934) is controlling.* In New York Trust, an individual purchased stock in 1906 and donated it to a trust on December 4, 1921. The trustee sold the property in 1922 at a price greater than either the transferor's basis or the value of the shares on the date transferred to the trust. Under the applicable Federal Revenue Act, the transfer to the trustee was not taxable, and the trustee assumed the donor's basis. The gain derived from the trustee's subsequent sale was to be taxed as ordinary income unless the shares were "capital assets", defined as "property acquired and held by the taxpayer . . .for more than two years." Revenue Act of 1921, §206(a) (6), 42 Stat. 227. The issue, therefore, was whether the trustee was to be treated as having constructively held the property for more than two years. There was no Federal tax statute in point.

The Supreme Court noted that "the time between the creation of the trust and the sale was less than the specified period [two years] and, if the words alone are to be looked to, the shares were not by the taxpayer 'held . . .for more than two years'." Id. at 463. The Supreme Court nevertheless held that the donor's holding period should be tacked to the trustee's, since any other result would be "unreasonable," "lacking in harmony," and "plainly at variance with the policy of the legislation as a whole." In language fully applicable to the case at bar, the Court explained that:

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*Although fully briefed by petitioners, the New York Trust case was not cited in the panel's opinion.

"Here the taxable gain was ascertained by putting together the periods in which the shares were held by trustor and trustee respectively. The taxable gain was the same as if the former held continuously from the time of purchase in 1906 until the sale in 1922. But to ascertain the applicable rate the Commissioner broke the continuity. If the trustor had held until the sale, the [capital gain rate] would have been applicable and the tax would have been substantially less than one-fourth of the amount assessed against the trustee who, for the purpose of calculating the gain, was substituted for the trustor.

"Sections 202(a) (2) and 206(a) (6)* are included in the same Act and are applicable respectively to different elements of the same or like transactions and are not to be regarded as wholly unrelated. While undoubtedly legally possible and within the power of Congress, <u>the methods adopted and results attained by the Commissioner are so lacking in harmony as to suggest that the continuity required to be used to get the base was also intended for use in finding the rate. No valid ground has been suggested for requiring tenures to be added for the one purpose and forbidding combination for the other</u>. The legislative purpose to be served by the application of the lower rate upon capital gains is directly opposed to the Commissioner's construction. There is no ground for discrimination such as that to which the trustee was subjected. It is to be inferred that Congress did not intend penalization of that sort." [Emphasis added.]

<u>Helvering</u> v. <u>New York Trust Company</u>, <u>supra</u>, is indistinguishable from the case at bar. In both cases:

(1) The taxpayer acquired property in a non-taxable transaction;

(2) The taxpayer's basis for determining gain was his transferor's basis, because the property was acquired in a non-taxable transaction;

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*Section 202(a) (2) provided: "That the basis for ascertaining the gain derived . . . from a sale. . .of property. . . shall be the cost of such property; except that . . .(2) in the case of such property, acquired by gift. . .<u>the basis shall be the same as that which it would have in the hands of the donor</u>." (Emphasis added.) Section 206(a) (6) defined capital assets as: ". . .property acquired and held by the taxpayer . . . for more than two years."

(3) Whether the property was a capital asset depended upon whether it was "held . . . for more than 2 years";

(4) The taxpayer would not have been deemed to have "held the property for more than 2 years," unless there was included in his holding period the period during which the property was held by the transferor; and

(5) There was no statutory language specifically requiring or forbidding the tacking of holding periods.

Amicus curiae submits that the logic which impelled the Supreme Court to tack holding periods in New York Trust requires that the petitioners in the present case be allowed to include the corporation's holding period in their own. The same dates must be used for calculating a taxpayer's holding period as for calculating his gain.

The salient aspect of New York Trust is that the Supreme Court found tacking to be compelled not by any statutory provision, but by the logic and fairness which should be inherent in any scheme of taxation. New York Trust was based not upon statutory language peculiar to Federal law, nor, indeed, upon any statute at all. It was predicated upon "the common law of taxation" and is therefore controlling authority for tacking in the instant case.

Even before the New York Trust decision, the Treasury Department, by regulation, had recognized as a basic tax principle the carryover of holding period in cases involving a carryover of basis. Regs. 62, Art. 1651 (Revenue

Act of 1921); Regs. 65, Art. 1651 (Revenue Act of 1924). See, also I.T. 1765, II-2 C.B. 44 (1923). Since the Federal tax legislation then in effect, like the present District of Columbia Income and Franchise Tax Act, was silent with respect to tacking, these early Treasury Department regulations manifestly reflect concepts of fundamental fairness in the administration of an income tax system - concepts fully applicable to the District income tax law.

When this administrative practice was codified in Section 208 (a) (8) of the Revenue Act of 1926, 44 Stat. 9, Congress made clear that its purpose in enacting that section was to clarify and give statutory recognition to existing tacking policy. H. Rept. No. 1, 69th Cong., 1st. Sess., p. 6, 1939-1 CB (Part 2) 319 provides in pertinent part as follows:

> "Section 208(a)8: The 12-1/2 per cent capital gain and loss provisions apply only to the sale or exchange of capital assets which have been held by the taxpayer for two years. Under the reorganization provisions many transactions are exempt from tax until the stockholder disposes of his stock received as a result of the reorganization. As a result of this fact the question frequently arises as to whether the period that the taxpayer held the stock which he exchanged for new stock should be added to the period for which he held his new stock, in order to determine whether or not he has held it for two years. The amendment proposed to this section incorporates in the law the present regulation of the Treasury and provides that these two periods shall be added for the purpose of determining the period during which the property sold was held for the purpose of determining both gain and loss under this section. The same question arises in the case of property received by gift after December 31, 1920. The amendment provides that the period in which the property was held by the donor shall be added to the

> period in which the property was held by the donee in determining whether or not the property so received falls within the capital gain or loss section." (Emphasis added.)

This rule has been given application in a variety of non-taxable transactions. See, Vol. 3, Mertens, Law of Federal Income Taxation, §§22.105 - 113a (1966 rev.).

Applying the common law principle articulated by the Supreme Court in the New York Trust case, reflected in the early administrative decisions under a statute containing language identical to that before the Court herein and embodied in the Internal Revenue Code since 1926, the phrase "held by the taxpayer" in D.C. Code §47-1557 c (1) must be construed to embrace the tacking of holding periods. See, District of Columbia v. A.C.F. Industries, Inc. 122 U.S. App. D.C. 12, 15, 350 F.2d 795 (1965) ("Where no policies appear to require otherwise, we have generally, if implicitly, assumed that Congress intended similar construction of both the local and federal tax statutes, thus recognizing the practical convenience gained from having similar tax rules."); District of Columbia v. Lewis, 109 U.S. App. D.C. 353, 288 F.2d 137 (1961).

The panel's decision in the case at bar appears to have been based on a misconception of the tacking principle. The majority opinion held that "neither the period a corporation holds distributed property nor the period a stockholder holds his stock in the distributing corporation is the criterion in the District for measuring the duration of his ownership to ascertain whether for him it is a capital asset." Verkouteren v. District of Columbia, ______ U.S. App.

D.C. ______, ________F.2d________(February 6, 1969, Slip. Op. p. 10). The opinion, however, does not mention tacking or the New York Trust case, but instead reasons that "Capitol was not the *alter ego* of its shareholding community, but a tax entity distinct from its stockholders." Slip. Op. at 8. In other words, the panel viewed petitioners' argument as an effort to pierce the corporate veil or otherwise trespass upon the separate legal identities of a corporation and its shareholders. The tacking doctrine, however, is consistent with the separate legal identity of shareholder and corporation. It is the reasonable and necessary counterpart of the tax rule which requires that the basis of property acquired from a wholly separate transferor be carried over (not stepped-up) when the acquisition was not a taxable transaction. In other words, tacking is required because without it a taxpayer would be taxed on another's unrealized gain but denied his holding period, not because of any control by the taxpayer over his transferor or identity of interest and ownership between the parties. It follows that the decision of the panel denying tacking was in error, and that the petitioners must be deemed, for tax purposes, to have held the Chastleton stock since its acquisition by Capitol. Accordingly, the Chastleton stock was a capital asset in the hands of petitioners, and any gain realized upon the subsequent sale was exempt from taxation under D.C. Code §47-1557a (b) (11).

CONCLUSION

Amicus curiae respectfully submits that this Court should order that the deficiency arising from taxation of the Chastleton stock sale assessed against and paid by petitioners be refunded because such stock had: (1) a basis equal to its cost to the corporation, and (2) a holding period, in the shareholders' hands, of more than two years beginning with acquisition by the corporation.

Respectfully submitted,

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PETITIONERS' PETITION FOR REHEARING
AND SUGGESTION FOR REHEARING IN BANC

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Petition for Review of a Decision of the
District of Columbia Tax Court

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PETITIONERS' PETITION FOR REHEARING
AND SUGGESTION FOR REHEARING *IN BANC*

This case, *John H. Verkouteren, et. al.* v. *District of Columbia*, was decided by a panel of this Court on February 6, 1969 in an opinion by Judge Robinson in which Judge Fahy joined. Judge Leventhal dissented in a separate opinion.

Petitioners, by their attorneys Albert E. Arent and Joel N. Simon, respectfully request a rehearing before the panel of this Court (Judges Robinson, Fahy and Leventhal) which decided this case. Alternatively, Petitioners respectfully suggest that this Court order a rehearing _in banc_ in this case. This case should be reheard, either by the panel that decided it or _in banc_, for the reasons set forth below.

I.

THE MAJORITY OPINION IN THIS CASE IS IN DIRECT CONFLICT WITH THE DECISION OF A DIFFERENT PANEL OF THIS COURT IN AN EARLIER CASE

The basic issue in this case is determining the basis for District of Columbia income tax purposes of appreciated property received by the shareholders of a corporation which has liquidated and has distributed to its stockholders all of its assets. The majority opinion in this case held that the stockholders' basis for the corporate assets received as a liquidating distribution was equal to the book value (_i.e._, the original cost) of the assets in the hands of the corporation. This decision is in direct conflict with the decision of a different panel of this Court (Judges Prettyman, Tamm and Leventhal) in the case of _Snow_ v. _District of Columbia_, 124 U.S. App.

D.C. 69, 361 F.2d 523 (1965), <u>rehearing en banc denied</u> (1966).*
In <u>Snow</u>, the Court specifically rejected the use of the corporation's book value as the basis for the assets received by the stockholder and held instead that the stockholder's basis for the corporate assets received as a liquidating distribution was equal to the value of the stock he turned in to receive the distributed property. In contrast, in this case the majority opinion - without discussing <u>Snow</u> - specifically rejected the approach used by the Court in <u>Snow</u>.

A brief comparison of this case and the <u>Snow</u> case will highlight the patent inconsistency between them.

<u>This Case</u>	<u>The Snow Case</u>
<u>Facts</u>	
Stockholder-petitioners owned three-fifths of the stock of Capitol Hotel Enterprises, Inc. ("Capitol"), a corporation.	Stockholder Snow owned all of the stock of Lombardy, Inc. ("Lombardy"), a corporation.
* *	*
Capitol's principal asset consisted of the stock of a second corporation, Chastleton Hotel, Inc. ("Chastleton stock"), with a book value on Capitol's books of $20,480.	Lombardy's principal asset consisted of an apartment house with a book value of $271,000. It also owned other assets with a book value of $300,000.

*Judge Leventhal, though a member of the panel, did not participate in the consideration of the <u>Snow</u> case.

This Case	The Snow Case
Capitol also owned other assets with a book value of $80,500.	
*	* *
Capitol was liquidated and its assets, including the Chastleton stock, were distributed to its stockholders. As shareholders, Petitioners received three-fifths of the assets distributed.	Lombardy was liquidated and its assets, including the apartment house, were distributed to Snow, its sole stockholder.
*	* *
At the time of Capitol's liquidation, the fair market value of its assets was $470,500. The Chastleton stock had a fair market value of $390,000.	At the time of Lombardy's liquidation, the fair market value of its assets was $1,000,000. The apartment building had a fair market value of $700,000.

<u>Holding</u>

This Case	The Snow Case
Petitioners' basis for the Chastleton stock is $12,288, which is an amount equal to their three-fifths share of the $20,480 book value of the Chastleton stock on Capitol's books (slip opinion, pages 13-14; footnote 36). "We cannot accept the proposition that the market value of the Capitol stock which	Stockholder Snow's basis for the apartment house is the "proper proportion of . . . [his] cost . . ., which is the value of the stock he turned over for the property." 124 U.S. App. D.C. at 73, 361 F. 2d at 527. Since the value of the stock Snow "turned over" was $1,000,000, the basis of the apartment building was $700,000, its fair market value.

This Case	The Snow Case
petitioners relinquished upon Capitol's dissolution represented their cost of the Chastleton stock which they then obtained and later sold." (slip opinion, page 11).	

* * *

There are two possible ways in which it could be argued that the obvious inconsistency between this case and the Snow case might be reconciled. First, there is a factual difference between this case and Snow in that in the latter case Mr. Snow purchased the stock of Lombardy for $1,000,000 and then caused Lombardy to be liquidated. However, this factual difference was not relied upon to any extent in the Snow opinion as a justification for the result. Judge Prettyman's decision in Snow is based on an exhaustive analysis of the nature of a corporate liquidating distribution under the District's tax law. He analyzed this Court's earlier decision in Berliner v. District of Columbia, 103 U.S. App. D.C. 351, 258 F.2d 651, cert. denied. 357 U.S. 937 (1958), which did not involve a change in stock ownership preceding the liquidation, and carefully delineated its perimeter. Since the significance of the change in stock ownership before the

liquidation was called to the Court's attention in Snow,* the Court's failure to adopt the change in beneficial ownership as a rationale for its decision eliminates this factual difference as a basis for reconciling the inconsistency between this case and Snow. Moreover, if a corporation and its shareholders are treated as separate entities for tax purposes, changes of stock ownership at the shareholder level should have no effect at the corporate level.

The second possible basis for distinction is that this case, which involves basis for determining gain or loss on sale, is governed by D.C. Code §47-1583, while the Snow case, which involved basis for depreciation, was governed by D. C. Code §47-1583e. Considering the anomalies already inherent in the "simultaneous application to the . . . [District of Columbia] taxpayer by the same legislature of two different sets of statutory provisions,"** it is even more frightening to contemplate the development by this Court of a ratio decidendi

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*See Judge Fahy's statement in support of granting the District of Columbia's petition for rehearing en banc, 124 U.S. App. D.C. at 74, 361 F.2d at 528.

**Slip opinion, page 15.

in which the same asset may have one basis for depreciation and an entirely differen' basis for determining gain or loss on sale. But if it is possible for an asset distributed to stockholders in a corporate liquidation to have one basis for determining gain or loss on sale and a different basis for depreciation, the likelihood is that the basis for determining gain or loss on sale -- the issue in this case -- will be greater than the basis for depreciation of such property, not the converse. See Judge Danaher's concurring opinion in Oppenheimer v. District of Columbia, 124 U.S. App. D.C. 221, 225, 363 F.2d 708, 712 (1965), rehearing en banc denied (1966).

For these reasons, Petitioners suggest that this case and Snow are antithetical and that one of them cannot stand.

THE MAJORITY OPINION RAISES AN IMPORTANT AND RECURRING QUESTION CONCERNING THE DEGREE TO WHICH, AND THE STANDARDS BY WHICH, FEDERAL TAX LAW IS TO BE APPLIED TO FILL THE GAPS IN THE DISTRICT'S TAX LAW

Petitioners' alternative argument in this case was that if their basis for the Chastleton stock was equal to Capitol's cost, then they should be entitled to add Capitol's twelve year holding

period to their own holding period in order to qualify the Chastleton stock as a capital asset.* Without even mentioning, much less distinguishing, Helvering v. New York Trust Co., 292 U.S. 455 (1934), which Petitioners relied on as persuasive authority on the issue of "tacking," the majority opinion held (slip opinion, page 10) that "neither the period a corporation holds distributed property nor the period a stockholder holds his stock in the distributing corporation" is to be considered in determining the holding period for property distributed in liquidation. Thus, in this case, the majority opinion rejected out of hand the precedents and analogies developed in over fifty years of experience in the Federal income tax law.

The District's tax law is completely silent on the question of "tacking." "Tacking" is a firmly established, fundamental principle of Federal tax law which has been applied even in the absence of statute. In rejecting Petitioners' "tacking" argument, the majority opinion ignored many other similar situations where Federal tax law principles and statutes have been applied to fill

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*D.C. Code §47-1551c(1) defines a "capital asset" as property held for more than two years. Gain from the sale of a "capital asset" is exempt from tax. D.C. Code §47-1557a(b)(11).

the void in the District's law. For example, in District of Columbia v. Lewis, 109 U.S. App. D.C. 353, 288 F.2d 137 (1961), this Court relied completely upon a specific definition of a phrase contained in the Federal statute in construing the same phrase (undefined) in the District's tax law, thus treating the Federal definition as if it were expressly a part of the District's law.

Similarly, in Mary Kaplan v. District of Columbia, CCH DC Tax Rep. ¶200-117 (D.C. Tax Ct., October 11, 1967), the Tax Court, faced with a case where "the [D.C.] statute imposing the income tax is silent as to who should claim deduction for depreciation in a situation like that here under consideration," applied the express provisions of section 167(h) of the Internal Revenue Code of 1954 to resolve the problem. Other examples abound in the reports of resort to Federal statutes and case law to add meat to the "skeletal provisions constituting the District of Columbia income tax law" (slip opinion, page 14, dissenting opinion).

From the majority opinion's outright rejection of Federal tax principles in this case one can only conclude that the majority is willing to countenance a selective application of Federal law to fill in the interstices of the District's law, but through a process

of selection wholly lacking in guidelines, touchstones or any other objective criteria to enable taxpayers, administrators or the courts to distinguish the cases where Federal law is to be applied from those where it is not. Why should Federal tax law be incorporated _in haec verba_ in the _Lewis_ and _Kaplan_ cases, but not in this case? This case, like the _Lewis_ and _Kaplan_ cases, involves a situation where the District's law is silent, not one where, as in the _Berliner_ case, _supra_, the District's law was clearly different from the comparable Federal law.

Certainly taxpayers and tax administrators alike are entitled to some explanation of the selection process -- other than selection by judicial fiat. Without further explanation, the majority's approach, if allowed to stand, must inevitably lead into a quagmire of confusion where any intelligible principles of law will quickly sink into oblivion. The majority opinion is, therefore, a standing invitation to chaos in the interpretation of the District's income tax law, and a rehearing by the panel or _in banc_ should be granted to resolve this question of exceptional importance to the proper administration of the District's tax law.

THE MAJORITY OPINION IS INTERNALLY INCONSISTENT AND IS BASED ON AN ERRONEOUS ASSUMPTION OF FACT

The applicable statute requires that Petitioners' basis for determining gain from the sale of the Chastleton stock "shall be the cost of such property." D.C. Code §47-1583. The majority opinion in this case holds that Petitioners' cost for the Chastleton stock is equal to their three-fifths of the book value of the Chastleton stock on Capitol's books (slip opinion, pages 13-14). But how can this holding be reconciled with the Court's earlier statement (slip opinion, page 8) that "Capitol was not the alter ego of its shareholding community, but a tax entity distinct from its stockholders"? If Capitol and its stockholders were separate tax entities -- and we believe they were -- how can Capitol's cost for the Chastleton stock be Petitioners' cost? Alternatively, if Capitol's cost for the Chastleton stock is Petitioners' cost -- as the majority held in this case -- why is Capitol's 12-year holding period for the Chastleton stock not added to Petitioners' holding period, so that the Chastleton stock qualifies as a capital asset in Petitioners' hands?

The majority opinion in this case holds (slip opinion, page 13) that "the stockholders' [Petitioners'] true and only cost of that stock [the Chastleton stock] was the $20,480 portion of the taxable

liquidating dividend that was attributable to the Chastleton stock." (Emphasis added). We respectfully submit that the excerpt from the majority opinion quoted above, which reflects the rationale permeating the entire majority opinion, involves a most fundamental misconception of the nature of "earned surplus."

Earned surplus is not in any true sense attributable to any particular corporate asset, but represents an accounting convention which is useful in describing the amount by which total corporate capital exceeds the capital invested by the stockholders. A basic assumption of the majority opinion is that a portion of Capitol's earned surplus was "attributable to the Chastleton stock" so that this portion became Petitioners' cost basis for the Chastleton stock upon Capitol's liquidation. But the facts of this case do not support this assumption. What the majority overlooked is that Capitol, when it was formed in 1948, acquired the Chastleton stock and continued to own it until its (Capitol's) liquidation in 1960. From this it must be obvious that Capitol's earned surplus was not "attributable to" the Chastleton stock, because Capitol still owned the Chastleton

stock when it liquidated. Capitol's earned surplus must have been "attributable to" its other assets, and treating a portion of this earned surplus as Petitioners' cost for the Chastleton stock is an arbitrary and artificial result which bears no relationship to the economic facts.

WHEREFORE, Petitioners request that the foregoing petition be granted.

Respectfully submitted,

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Date: February, 1969

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BRIEF FOR PETITIONERS AND JOINT APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 20,889 - 20,894

JOHN H. VERKOUTEREN, ET AL.,

Petitioners,

v.

DISTRICT OF COLUMBIA,

Respondent.

Petition for Review of a Decision of the
District of Columbia Tax Court

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QUESTIONS PRESENTED

1. Whether the District of Columbia Tax Court erred in failing to determine that Petitioners' cost basis for the capital stock of Chastleton Hotel, Inc., received by them upon the liquidation of Capitol Hotel Enterprises, Inc., was equal to the fair market value of the common stock of Capitol which they surrendered therefor.

2. Whether, assuming that the District of Columbia Tax Court was correct in requiring that the cost basis to Petitioners for the capital stock of Chastleton Hotel, Inc., be determined by reference to its cost basis to Capitol Hotel Enterprises, Inc., the District of Columbia Tax Court erred in refusing also to determine the Petitioners' holding period for the capital stock of Chastleton Hotel, Inc., by including the period of time during which such stock was held by Capitol Hotel, or whether, in the alternative, the District of Columbia Tax Court erred in refusing to determine the Petitioners' holding period for the capital stock of Chastleton Hotel, Inc., by including the period of time during which the Petitioners held their stock in Capitol Hotel.

3. Whether, in the alternative, the District of Columbia Tax Court erred in failing to allow Petitioners to use as the cost basis for the capital stock of Chastleton Hotel, Inc., received by them, that portion of the amount of the liquidating distribution treated as a dividend which the fair market

value of the capital stock of Chastleton Hotel, Inc., bore to the fair market value of all property distributed in liquidation by Capitol Hotel Enterprises, Inc.

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UNITED STATES COURT OF APPEALS
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v.

DISTRICT OF COLUMBIA,

Respondent.

Petition for Review of a Decision of the
District of Columbia Tax Court

BRIEF FOR PETITIONERS

JURISDICTIONAL STATEMENT

These consolidated cases are petitions pursuant to D. C. Code § 47-2404 to review decisions on remand of the District of Columbia Tax Court (Morgan, J.) entered on November 10, 1966, which decisions affirmed the deficiencies in income tax assessed by the District of Columbia against the respective Petitioners for the calendar year 1960 and determined that the respective Petitioners were not entitled to any refund thereof (J.A. 24-29). The Tax Court's original decisions in these cases were entered on March 4, 1964. Subsequently, this Court, in a decision published

in 120 App. D. C. 361, 346 F. 2d 842 (May 11, 1965), reversed the decisions of the Tax Court and remanded these cases back to the Tax Court for further proceedings. The Tax Court entered its Findings of Fact and Opinion on Remand on November 10, 1966 (J.A. 17). On November 16, 1966, the Petitioners filed in the Tax Court a motion to revise the opinion (J.A. 30). On February 2, 1967, the Tax Court entered a Memorandum and Orders denying Petitioners' motion (J.A. 31-35). On February 28, 1967, Petitioners filed in the Tax Court petitions to this Court to review the Decisions on Remand of the Tax Court (J.A. 35).

These consolidated cases are actions for a refund of income tax assessed by the District of Columbia for the calendar year 1960 in the total amount of \$13,906.61, together with interest of \$1,807.86. The Tax Court had jurisdiction pursuant to D. C. Code § 47-1593.

STATEMENT OF THE CASE

On November 14, 1963, a Stipulation of Facts was filed with the Tax Court in connection with the above-entitled cases covering all pertinent facts believed necessary to a dispostiion of these cases (J.A. 11-16). The revelant facts, as set forth in the Stipulation, may be briefly summarized as follows:

Capitol Hotel Enterprises, Inc. (hereinafter referred to as "Capitol"), was organized in 1948 under the laws of the State of Delaware. Thereafter, in the same year, Capitol purchased 200 shares of Preferred Stock and 480 shares of Common Stock of Chastleton Hotel, Inc., a Delaware corporation,

for $20,000 and $480, respectively. For convenience in identification, the Preferred Stock and the Common Stock of Chastleton Hotel, Inc., will hereinafter be referred to in the aggregate as the "Chastleton Stock." From its organization in 1948 until January 29, 1960, Capitol's business consisted of the ownership and management of investment properties (Stip. Pars. 10, 11, J.A. 13).

On January 29, 1960, Capitol was dissolved under applicable Delaware law. On that date, immediately prior to its dissolution, the book value of Capitol's assets and net worth were as follows:

Assets		Net Worth	
Chastleton Stock	$ 20,480.00	Capital Stock	$ 1,200.00
Other unrelated assets	80,541.30	Earned Surplus	99,821.30
	$101,021.30		$101,021.30

The fair market value of the Chastleton Stock on January 29, 1960, was $390,000 and the fair market value of its other unrelated assets on that date was $80,541.30 (Stip. Par. 11 and Ex. A, J.A. 14, 16).

Immediately prior to Capitol's dissolution, each of the individual Petitioners owned, and had owned since 1948, the number of shares of Capitol's common stock indicated in Paragraph 10 of the Stipulation (J.A. 13). Upon the dissolution of Capitol, each of the Petitioners received, in complete cancellation and redemption of the Capitol common stock owned by him, an interest in the Chastleton Stock and the other unrelated assets owned by Capitol prior to dissolution proportionate to his Capitol common stock.

The number of shares of Chastleton Stock received by each Petitioner is set forth in Paragraph 12 of the Stipulation (J.A. 14).

On February 1, 1960, each of the Petitioners sold the Chastleton Stock received by him on the dissolution of Capitol for the amount and on the terms set forth in Paragraph 13 of the Stipulation (J.A. 14-15).

On the District of Columbia Income Tax Return filed by each Petitioner for the year 1960 no amount was shown as a dividend from Capitol or as a gain on the sale of the Chastleton Stock. Upon examining Petitioners' 1960 Income Tax Returns, the District of Columbia (hereinafter referred to as the "District") adjusted the tax liability of each Petitioner by adding to each Petitioner's reported taxable income a dividend from Capitol equal to his pro rata share of Capitol's Earned Surplus ($99,821.30) prior to dissolution, and an amount of Petitioner's pro rata share of purported taxable gain on the sale of the Chastleton Stock. These respective amounts are set forth in Paragraph 9 of the Stipulation (J.A. 12). The amount of each Petitioner's share of the purported taxable gain on the sale of the Chastleton Stock was computed by allocating to each Petitioner, as his cost basis for the Chastleton Stock received by him on dissolution, his pro rata share of Capitol's aggregate cost basis ($20,480) for the Chastleton Stock so distributed (Stip. Pars. 7, 8, 9; Petitions, Ex. B, J.A. 2, 7-9, 13).

On May 17, 1963, the District assessed deficiencies against each Petitioner with respect to his pro rata shares of the dividend from Capitol and the purported gain on the sale of the Chastleton Stock. These deficiencies,

together with interest thereon, were paid by Petitioners between June 1-15, 1963 (Stip. Par. 8, J.A. 12). On August 13, 1963, each Petitioner filed a petition in the Tax Court appealing from the assessment of income tax against him and requesting a determination that he was entitled to a refund of the tax and interest paid (J.A. 2-10).

On March 4, 1964, the Tax Court filed its Findings of Fact and Opinion and its Decisions affirming the assessments against Petitioners. This Court, in the case of Verkouteren v. District of Columbia, 120 App. D. C. 361, 346 F. 2d 842 (May 11, 1965), reversed the decisions of the Tax Court and remanded these cases back to the Tax Court for further proceedings. The Tax Court entered its Findings and Fact and Opinion on Remand and its Decisions on Remand on November 10, 1966 (J.A. 17-29). On November 16, 1966, the Petitioners filed in the Tax Court a motion to revise the opinion (J.A. 30). On February 2, 1967, the Tax Court entered a Memorandum and Orders denying Petitioners' motion (J.A. 31-35). On February 28, 1967, Petitioners filed in the Tax Court petitions to this Court to review the Decisions on Remand of the Tax Court (J.A. 35).

STATUTES INVOLVED

The pertinent statutes are set forth in the Appendix, infra.

STATEMENT OF POINTS

Petitioners rely upon the following points in this case:

1. The District of Columbia Tax Court erred in determining that Petitioners' cost basis for the Chastleton Stock received by them upon

the liquidation of Capitol was not equal to the fair market value of the common stock of Capitol which they surrendered therefor.

2. The District of Columbia Tax Court determined Petitioners' cost basis for the Chastleton Stock either by reference to Capitol's cost basis for the Chastleton Stock or by reference to Petitioners' cost basis for their common stock in Capitol. Assuming that the District of Columbia Tax Court's determination of basis was correct, then the Tax Court erred in refusing also to determine the Petitioners' holding period for the Chastleton Stock either by reference to the period of time in which Capitol held the Chastleton Stock or by reference to the period of time in which Petitioners held their common stock in Capitol.

3. In the alternative, the District of Columbia Tax Court erred in failing to allow Petitioners to use as the cost basis for the Chastleton Stock that portion of the amount of the liquidating distribution treated as a dividend which the fair market value of the Chastleton Stock bore to the fair market value of all property distributed in liquidation.

SUMMARY OF ARGUMENT

I. PETITIONERS DID NOT REALIZE TAXABLE GAIN UPON THE SALE OF THE CHASTLETON STOCK BECAUSE THE AMOUNT REALIZED BY THEM FROM THE SALE DID NOT EXCEED THEIR COST BASIS THEREFOR.

When properly construed in the light of its Federal counterpart, the D.C. Income Tax Act treats a corporate liquidating distribution as consisting of two distinct elements. First, to the extent of the distributing corporation's

earned surplus, it treats the distribution as a taxable "dividend." Second, any excess of the amount of the distribution over the amount treated as a "dividend" is regarded as being received in exchange for the underlying stock. Capitol's stockholders received a total liquidating distribution of approximately $470,000, consisting of the Chastleton Stock with a fair market value of $390,000 and other unrelated assets with a value of about $80,000. The entire distribution of $470,000 should be treated as consisting of a "dividend" of $99,821.30 (the amount of Capitol's earned surplus), a return of capital of $1,200 (the aggregate amount of the stockholders' basis for their Capitol stock) and a gain on the liquidation with respect to the balance of $367,000. Since the stockholders of Capitol held the underlying common stock of Capitol for more than two years, the gain on liquidation of $367,000 qualified as a gain from the sale or exchange of a capital asset and was, therefore, exempt from income tax under D. C. Code § 47-1557a (b)(11).

Subsequently, the stockholders of Capitol sold the Chastleton Stock for $390,000, an amount equal to its value on the date of Capitol's liquidation. The most significant portion of the $367,000 gain on liquidation realized by the stockholders upon the liquidation of Capitol--but not returned as income by them at that time because such gain was an exempt capital gain--was attributable to an appreciation in value of the Chastleton Stock. Since the manifest policy of the D.C. Income Tax Act is to treat this gain as exempt, it is essential, in order to effectuate this policy of exemption,

that the subsequent sale of the Chastleton Stock by the stockholders of Capitol not result in the imposition at that time of a tax on the gain which was previously treated as exempt. If, however, the stockholders of Capitol are treated, when they subsequently sold the Chastleton Stock, as then becoming subject to tax on the gain which upon their initial receipt of the property following Capitol's liquidation was treated as exempt, the statutory direction that the gain on liquidation be exempt from income tax will have been thwarted. Instead of the gain being exempt, the result will be that the gain on the liquidation is not exempt but its amenability to tax will have been deferred or postponed until a subsequent sale of the property. This, however, is not the meaning of exemption and is not a result dictated by the statute.

In order to further the policy of exemption manifested by the D.C. Income Tax Act--by not subjecting to tax upon a subsequent sale the exempt gain initially realized at the time of liquidation--the stockholders of Capitol should be treated as having received an aggregate basis for the property distributed by Capitol upon liquidation equal to $470,000. D.C. Code § 47-1583 provides that the basis for determining gain or loss from the sale of property shall be "the cost of such property." In the case of a liquidation, the "cost" of the property received is, under well-settled principles, equal to the value of the stock of the liquidating corporation which is surrendered in connection with the liquidation. Immediately prior to the liquidation, the stock of Capitol was worth at least $470,000. This stock

was surrendered in order to receive the assets of Capitol. The "cost" to the stockholders of Capitol of the assets received on liquidation of Capitol was, therefore, $470,000. When the Chastleton Stock was thereafter sold for $390,000, no gain resulted from the sale.

II. IF PETITIONERS' COST BASIS FOR THE CHASTLETON STOCK IS DETERMINED BY REFERENCE TO CAPITOL'S COST BASIS, THEN PETITIONERS' HOLDING PERIOD SHOULD ALSO INCLUDE CAPITOL'S HOLDING PERIOD. ALTERNATIVELY, IF PETITIONERS' COST BASIS FOR THE CHASTLETON STOCK IS DETERMINED BY REFERENCE TO PETITIONERS' COST BASIS FOR THE STOCK OF CAPITOL HOTEL SURRENDERED THEREFOR, THEN PETITIONERS' HOLDING PERIOD SHOULD ALSO INCLUDE THEIR HOLDING PERIOD FOR THE CAPITOL HOTEL STOCK.

The Tax Court refused to permit the stockholders of Capitol to use their "cost" as the basis for the assets received by them upon Capitol's liquidation. Instead, the Tax Court required the stockholders to use Capitol's "cost" basis for the Chastleton Stock as their "cost" basis. If the Tax Court was correct in requiring the use of Capitol's "cost" basis, it should also have permitted the stockholders to include in their holding period for the Chastleton Stock the twelve year period in which the Chastleton Stock was held by Capitol. As a fundamental, common law principle of income taxation, a carry-over in holding period is always associated with a carry-over in basis. This principle was recognized in the absence of statute by the United States Supreme Court and by early administrative interpretations of the Federal income tax law, and has become so firmly imbedded in the fabric of income taxation that it must be deemed to have been incorporated

in the D.C. Income Tax Act. After giving effect to the carry-over of Capitol's twelve year holding period, Capitol's stockholders would be treated as having held the Chastleton Stock for more than two years, and the gain on sale should be an exempt capital gain.

Alternatively, if the stockholders' cost basis for the Chastleton Stock is not determined by reference to Capitol's cost basis therefor, then the only other rational method for determining the stockholders' basis is to treat the assets distributed in liquidation of Capitol as taking the place, in the hands of the stockholders, of the stock of Capitol owned by them before the liquidation. If the Chastleton Stock distributed in liquidation of Capitol is regarded as being received by the stockholders in substitution for the stock of Capitol, then the holding period for the Chastleton Stock distributed in liquidation should include the stockholders' twelve year holding period for their stock in Capitol, and the gain on a later sale of the Chastleton Stock should be an exempt capital gain.

III. AS AN ALTERNATIVE, THE DISTRICT OF COLUMBIA ERRED IN FAILING TO ALLOCATE PETITIONERS' COST BASIS FOR THE CHASTLETON STOCK ON THE BASIS OF THE AMOUNT OF THE DISTRIBUTION TREATED AS A TAXABLE DIVIDEND IN PROPORTION TO THE RESPECTIVE FAIR MARKET VALUES OF THE DISTRIBUTED PROPERTY.

In any event, the stockholders of Capitol should be entitled to a "cost" basis for the Chastleton Stock equal to that portion of the sum of Capitol's liquidating distribution treated as a "dividend" ($99,821.30) and Petitioners' cost basis for the stock of Capitol ($1,200), which the fair market value of

the Chastleton Stock ($390,000) bore to the fair market value of all assets distributed by Capitol upon its liquidation ($470,000). Capitol's entire distribution resulted in a "dividend" of $99,821.30. If the entire distribution is treated as giving the stockholders of Capitol an aggregate "cost" basis equal to the amount reported as a dividend plus their cost basis for the stock of Capitol ($1,200), then under established principles this aggregate basis should be apportioned among the component assets received in proportion to their respective fair market values.

ARGUMENT

These cases present the question of determining the basis, in the hands of the stockholders, of assets distributed in connection with a corporate liquidation. This is a question of great practical importance in the day-to-day administration of the D. C. income tax laws, as evidenced by the prolific litigation in this Court and in the lower courts which this issue has already produced. It appears at the present time that this issue is the most frequently controverted issue under the D. C. income tax laws and is involved in more pending cases, including cases pending at the administrative level in the D. C. Finance Office, as well as cases which have reached the litigation stage than any other single issue.

Unfortunately, conflicting decisions by different panels of this Court in Snow v. District of Columbia, ___ App. D.C. ___, 361 F.2d 523 (1965) (Judges Prettyman, Tamm and Leventhal), and in the "second Oppenheimer case," Oppenheimer v. District of Columbia, ___ App. D.C. ___, 363 F.2d

708 (1966) (Judges McGowan, Wright and Danaher), have cast serious doubt not only on the answer to the ultimate basis question, but also on the basic principles which form the framework for any analysis of the problem. Illustratively, although Snow and second Oppenheimer both involved the question of a stockholder's basis for assets received on liquidation of a corporation, Snow held that the basis of the property distributed on liquidation was equal to the value of the stock "turned over for the property," while second Oppenheimer held (without specifying what basis was) that the value of the stock surrendered by the stockholder in order to obtain the property did not determine the basis of the distributed property. Further confusion was created because Snow held that the portion of the assets of the liquidated corporation in excess of earned surplus were distributed to the stockholder in exchange for the underlying stock of the corporation; but second Oppenheimer held that a corporate liquidation did not involve any element of an exchange.

The doubt and uncertainty created by the conflicting decisions in Snow and second Oppenheimer have cast a shadow over many legitimate business transactions and threaten to make informed business and tax planning for corporate liquidations impossible. As a result, the issues raised by these cases deserve and require the deliberate and thoughtful attention of this Court. The facts of these cases present an ideal vehicle for this Court to resolve the conflict between the Snow and second Oppenheimer decisions.

I. PETITIONERS DID NOT REALIZE TAXABLE GAIN ON THE SALE OF THE CHASTLETON STOCK BECAUSE THE AMOUNT REALIZED BY THEM FROM THE SALE DID NOT EXCEED THEIR COST BASIS THEREFOR.

A. The Basis For Determining Gain On Sale Of Property Received As A Liquidating Distribution Is Equal To The Fair Market Value Of The Surrendered Stock Of The Liquidated Corporation.

D. C. Code § 47-1583a provides:

> (a) Computation of gain or loss. -- The gain or loss, as the case may be, from the sale or other disposition of property shall be the difference between (a) the amount realized from such sale or other disposition of the property and (b) the basis as defined in section 47-1583.

D. C. Code § 47-1583 provides:

> The basis for determining the gain or loss from the sale, exchange, or other disposition of property shall be the cost of such property * * *

Although no Regulations have been promulgated under the D. C. Income Tax Act construing the term "cost," Regulations promulgated under the comparable provisions of Federal income tax law define "cost" as "the amount paid for * * * property in cash or other property." Treas. Regs. § 1.1012-1(a). It has been held that where property is acquired by a corporation in exchange for the issuance of stock, the "cost" to the corporation of the property received by it is equal to the fair market value of the stock issued. Ambassador Petroleum Co., 28 B.T.A. 868 (1933), rev'd on other grounds, 81 F.2d 474 (9th Cir. 1936); Stires Corporation, 38 B.T.A.

1 (1933). Cf. Maltine Co., 5 T.C. 1265 (1945). In Estate of Myers, 1 T.C. 100 (1942), the Tax Court observed (p. 111):

> Just as the cost of property purchased for cash is the amount of money given for it, so it would seem to follow in a strict sense that the cost of property acquired in an exchange is what the recipient parts with, that is, the value of the property given in exchange.

In the instant case, before Capitol was liquidated each Petitioner owned shares of Capitol's common stock; and the total value of all common stock of Capitol was, of course, equal to the total value of Capitol's net assets. Each Petitioner's basis for the pro rata share of Capitol's assets which he received on liquidation was equal to his "cost," i.e., the fair market value of the shares of Capitol's common stock which he surrendered upon the liquidation of Capitol. The value of these shares of Capitol's common stock represented the amount which each Petitioner parted with in order to receive his pro rata share of Capitol's assets. Since, as already noted, the fair value of Capitol's common shares was equal to the total fair value of Capitol's assets, each Petitioner's cost basis for the assets of Capitol which he received on liquidation was equal to the respective fair market values of such assets. Petitioners' contention is squarely supported by A.R.R. 403, 4 C.B. 32 (1921), involving Section 202 of the Revenue Act of 1918,[1/] in which it was held that "in cases where there is a liquidation in

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1/ Section 202(a) of the Revenue Act of 1918, 40 Stat. 1059, provided, as does D. C. Code § 47-1583, that the basis of property is "cost."

kind the value of the thing received is to be used as the basis for computing profit upon subsequent sale thereof."

Furthermore, this Court's recent decision in Snow v. District of Columbia, supra, directly supports Petitioners' position. In Snow, the taxpayer had purchased all of the stock of a corporation and immediately after the purchase caused the corporation to be liquidated and its assets distributed to him. This Court held (361 F.2d 523, 527) that the taxpayer's basis for the distributed property was equal to his cost "which is the value of the stock he turned over for the property."

In these cases, immediately prior to the liquidation of Capitol, the total value of the common stock of Capitol owned by all shareholders was $470,541.30, as this was the aggregate value of all of Capitol's assets. Upon Capitol's liquidation, the shareholders surrendered common stock worth, in the aggregate, $470,541.30, receiving therefor assets worth, in the aggregate, $470,541.30. For the reasons discussed above, the shareholders' aggregate "cost" basis for these assets was $470,541.30, the value of the stock which they surrendered in order to receive the assets. Included in the assets so received was the Chastleton Stock, which, upon receipt, acquired a cost basis equal to its fair market value of $390,000. Since the Chastleton Stock was thereafter sold for $390,000, an amount not in excess of its cost basis to the selling shareholders, no taxable gain was realized on the sale.

B. <u>The Overriding Policy Of The D.C. Income Tax Act Exempting Capital Gains From Taxation Requires That The Basis For Sale Of Property Received As A Liquidating Distribution Be Equal To Its Fair Market Value.</u>

Petitioners contend that for purposes of the D.C. Income Tax Act, a liquidating distribution consists in part of a distribution of earned surplus, which is taxable to the shareholders as a dividend, and to the extent of the balance is a distribution of property in exchange for the underlying stock of the liquidating corporation. The latter portion of the liquidating distribution is taxable to the shareholder if his underlying stock is not a capital asset, but is an exempt capital gain if the underlying stock is a capital asset. Petitioners further contend that the manifest policy of the D.C. Income Tax Act exempting capital gains from taxation requires that the portion of the shareholder's gain on liquidation which is exempt as a capital gain must be reflected in an increased basis for the distributed property so that a subsequent sale by the shareholder of the distributed property will not result in the imposition of a tax upon the exempt capital gain.

At the outset, it must be admitted that the D.C. Income Tax Act is less than precise in its treatment of corporate liquidating distributions, and that there is no provision of the Act which is all-inclusive in its coverage. There are, however, several pertinent provisions of the Act which directly bear upon this problem.

First, D. C. Code § 47-1557a(a) defines the term "gross income," for purposes of taxation, as including --

> . . . income derived from any trade or business or sales or dealings in property, whether real or personal, other than capital assets as defined in this subchapter, growing out of the ownership, or sale of, or interest in, such property; also . . . gains or profits, and income derived from any source whatever.

Second, D. C. Code § 47-1551c(m) defines the term "dividend" as --

> . . . any distribution made by a corporation (domestic or foreign) to its stockholders or members, out of its earnings, profits, or surplus (other than paid-in surplus), whenever earned by the corporation . . . and whether distributed prior to, during, upon, or after liquidation or dissolution of the corporation: . . .

Finally, D. C. Code § 47-1557a(b)(11) provides a complete exemption from income tax for gains from the "sale or exchange of any capital assets." D. C. Code § 47-1551c(l) defines a "capital asset" as any property, with certain exceptions not pertinent, "held by the taxpayer for more than two years."

1. <u>The portion of a liquidating distribution in excess of the liquidating corporation's earned surplus is received in exchange for the underlying stock.</u>

In the recent decision in <u>Snow</u> v. <u>District of Columbia</u>, <u>supra</u>, a division of this Court unmistakably held that a liquidating distribution in excess of the liquidating corporation's earned surplus was received by the shareholder in exchange for the underlying stock. In <u>Snow</u>, the taxpayer had purchased all of the stock of Lombardy, Inc., for $1,000,000. Immediately after this purchase, Lombardy, Inc., was liquidated and its

assets, which had a fair market value of $1,000,000, were distributed to the taxpayer as its sole stockholder. Immediately prior to the liquidation, Lombardy, Inc., had earned surplus of $300,000. In accordance with this Court's prior decision in Berliner v. District of Columbia, 103 App. D.C. 351, 258 F.2d 651 (1958), cert. denied, 357 U.S. 937 (1958), the Court in Snow held that to the extent of the corporation's $300,000 of earned surplus, the distribution resulted in a taxable dividend. However, the Court also held that the taxpayer was entitled to a loss deduction because, after reducing the liquidating distribution by the amount taxable to him as a dividend, he received only $700,000 of his original stock investment of $1,000,000.

Although the Court in Snow does not state in so many words that the $700,000 distribution in excess of earned surplus was in exchange for the taxpayer's stock, the exchange rationale permeates the entire opinion. First, the Court (361 F.2d 523, 524-5) at great length distinguished its prior decision in Berliner v. District of Columbia, supra, noting that the Berliner case cannot be read as establishing the broad principle that a liquidating distribution is not, under any circumstances, to be treated as having been received in exchange for the underlying stock. On the contrary, Judge Prettyman went out of his way to point out that the no-exchange holding in Berliner applied only to the distribution of accumulated earnings (361 F.2d 523, 524-525):

> The District says that in Berliner, supra, we specifically determined that receipt by a District

> taxpayer of a liquidating dividend upon corporate dissolution does not constitute a sale or exchange of his stock. We did not so hold. That opinion was meticulous in repeatedly pointing out that we were dealing with a distribution of earnings, an earned surplus. * * * (Emphasis supplied.)

Second, the Court in Snow (361 F.2d 523, 526) stressed the fact that the stock of Lombardy, Inc., was not a capital asset because the taxpayer had held it for less than two years [D.C. Code § 47-1551c(1)], and therefore his loss was a fully deductible, non-capital loss. If the Court had not regarded this aspect of the transaction as an exchange, there would have been no need to stress the fact that the stock was not a capital asset. D. C. Code § 47-1557b(a)(4)(B) allows as a deduction from gross income any loss "incurred in any transaction entered into for the production . . . of income." Only capital losses, which result from the sale or exchange of capital assets, are non-deductible. See D. C. Code § 47-1557b(b)(6).

The Snow case is also significant because, in recognizing that a loss deduction may result from a liquidation, it serves as a touchstone for analyzing the effect on a shareholder of his receipt of the portion of a liquidating distribution which is not a dividend. A simple example will illustrate the problem. A purchases for $10,000 all of the stock of X Corporation, which has as its sole asset land then worth $10,000. X Corporation has, at the time of the purchase, earned surplus of $1,000. One year later, after the land has been rezoned and is worth $20,000, X Corporation is liquidated and the land is distributed to A, its sole shareholder. Assuming that X Corporation's earned surplus at the time of liquidation

is still $1,000, the liquidating distribution clearly results in a dividend to A of $1,000. However, in addition to the $1,000 dividend, A has also received in the liquidation other property worth $19,000, while his stock basis is only $10,000. Just as in Snow, where the taxpayer was entitled to a loss deduction of $300,000 because the $700,000 non-dividend distribution was less than his $1,000,000 stock basis, the conclusion is inescapable that in the above example A realizes $9,000 of income because he received a non-dividend distribution of $19,000 and had only a $10,000 basis for his stock. The Snow case itself demonstrates the correctness of this analysis:

> It has been suggested that the distribution of corporate assets in return for the corporate stock, i.e., a corporate liquidation, is not a "tax event", meaning that no tax effect flows from such an action. But the argument will not withstand examination and, if sustained, would, it seems to us, greatly embarrass the tax authorities. Surely the District would impose a tax upon a gain derived from such a transaction. If Snow had paid only $500,000 for the stock, surely the District would urge that when he received $700,000 for that stock he owed a tax on $200,000. Indeed its counsel admitted as much in oral argument. The statute neither states nor implies a different disposition of non-capital gains and non-capital losses in the computation of taxable net income. Under the statute, if a non-capital gain is to be included in net income in a certain transaction, a loss upon the same sort of transaction is to be included in the computation. (Emphasis supplied.) (Footnote omitted.) Snow v. District of Columbia, supra, at pp. 526-527.

The above example, of course, assumed that A held his stock in X Corporation for less than two years, so that the stock did not qualify as

a capital asset. If, however, A held the stock of X Corporation for more than two years before the liquidation, the effect of the liquidation on A would be considerably different, and it is this difference which puts the problem of the present cases in proper perspective. If, in the above example, A had held his stock for more than two years at the time of the liquidation, the liquidating distribution would still result in a dividend to A to the extent of the corporation's earned surplus of $1,000. Berliner v. District of Columbia, supra. However, the $19,000 non-dividend portion of the liquidating distribution would not result in any taxable gain to A, even though it exceeded his $10,000 stock basis, because A's stock, having been held for more than two years, would be a capital asset and this gain (i.e., the excess of $19,000 over $10,000) would be received by A in exchange for his stock and would, therefore, be an exempt capital gain.

Petitioners recognize that there is no decided case directly so holding. But Petitioners submit that this result inexorably follows from the reasoning in the Snow case. There appears to be no doubt that if the taxpayer in Snow had not liquidated the corporation immediately after purchasing the stock, but had instead waited for more than two years to do so, his loss would not have been deductible because the underlying stock would have become a capital asset. Likewise, if in the hypothetical gain case discussed in Snow, which is quoted above, the liquidation occurred more than two years after purchase of the stock, the gain would be an exempt capital gain.

Moreover, we believe that our analysis of the exempt capital gain that results from the non-dividend portion of a liquidating distribution where

the underlying stock is a capital asset, has in practice been recognized by the District of Columbia in the position it has consistently taken in the numerous liquidation cases that have been involved in litigation since *Berliner*. There has been no reported decision in a liquidation case in which the District of Columbia has ever attempted to impose a tax on the gain attributable to the excess of the non-dividend part of a liquidating distribution over the shareholder's stock basis, where the underlying stock was held for more than two years.

Even in the celebrated "first" *Oppenheimer* case, 2/ the District of Columbia did not argue for taxation at the shareholder level on this basis. In the first *Oppenheimer* case, this Court rejected the argument that the unrealized appreciation in value of a corporation's assets was realized by the corporation when it made a liquidating distribution. Since the unrealized appreciation in value was not realized by the corporation, it could not be included in the corporation's earned surplus and taxed to the shareholders as a dividend. The first *Oppenheimer* case stands for that proposition, but no more. It does not in any way deal with the question whether the unrealized appreication in value is realized by the shareholders upon their receipt of the liquidating distribution, not as dividend income, but under the general definition of gross income which includes "income derived from any source whatever." D. C. Code § 47-1557a(a). That question was neither argued

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2/ *District of Columbia* v. *Oppenheimer*, 112 App. D. C. 239, 301 F. 2d 563 (1961).

by the District nor considered by this Court in the _Oppenheimer_ case, presumably for the reason that the taxpayer in the _Oppenheimer_ case had held her stock in the liquidating corporation for more than two years so that any gain (in excess of the earned surplus treated as a dividend) would have resulted from an exchange and would have been an exempt capital gain.

The history of the Federal income tax law, in the image of which the District's income tax law was framed, indicates that a corporation and its shareholders have always been treated as separate and distinct taxable entitles. _Moline Properties, Inc._ v. _Commissioner_, 319 U. S. 436 (1943). As a result, it is a fundamental principle that in a corporate liquidation a shareholder does _realize_ income (or gain) measured by the excess of the fair market value of the property received over the cost basis for his stock. Treas. Regs. § 1.331-1(b); Treas. Regs. § 1.1001(a). Bittker & Eustice, Federal Income Taxation of Corporation and Shareholders (2nd ed., 1966), Sec. 9.01, _et seq._ Nothing in the District of Columbia income tax law indicates otherwise, and any other holding would be inconsistent with D. C. Code § 47-1557a, which defines "gross income" as including "income derived from any source whatever." In this regard, it is significant to note that the United States Supreme Court, for analogous pruposes of the Federal tax laws, has held that the term "gross income" was intended "to bring the taxing power to bear upon all receipts constitutionally taxable." _Commissioner_ v. _Glenshaw Glass Co._, 348 U.S. 426, 433 (1955).

The purpose of this discussion has been to demonstrate that, as recognized by this Court in Snow, under a proper analysis of the D. C. Income Tax Act a liquidating distribution consists of two separate and distinct parts.[3/] The first part is the part of the distribution which is treated as a dividend. It is determined solely by reference to the accumulated earnings of the corporation immediately prior to liquidation. The second part of the distribution is the part representing a sale or exchange of the underlying stock, and consists of the remainder of the liquidation proceeds. With respect to the former, the recipient stockholder reports a dividend and pays a tax thereon. But as to the latter, since this part is received in exchange for the underlying stock, any gain realized by the stockholder in excess of the cost basis for his stock is a capital transaction and, if he has held his stock for more than two years, the gain will qualify as a capital gain and be exempt from the D. C. Income Tax. This result, as applied to the instant case, is implicit in the fact that while the Petitioners received property worth approximately $470,000 as a liquidating distribution, the District sought to impose a tax only on the amount of the distribution which represented a dividend. As a result of the liquidation, Petitioners received

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3/ In Snow v. District of Columbia, supra, the Court of Appeals stated (361 F.2d 523, 526): "Distributions by a corporation may be (1) from its earnings, (2) from an increased value of its assets or some of them, or (3) a return to stockholders of that which they had put into the venture. The first two are gains to the stockholder, separated from the body of his investment by the act of distribution. The third is not a gain but is a return of what the stockholder already had, and so is not income. These principles have been prodigiously productive of litigation."(Emphasis supplied.)

property worth approximately $470,000, surrendered capital stock having a cost basis of $1,200, but were taxed on only a dividend equal to their respective shares of the corporation's earned surplus of approximately $99,000. The only explanation for not taxing the Petitioners upon the excess of the amount received as a liquidating distribution over the amount of the distribution treated as a dividend is that such excess was received in exchange for the underlying stock. Since the Petitioners had held the underlying stock for more than two years, the stock was a capital asset [D. C. Code § 47-1551c(1)] and the gain resulting from an exchange of the stock was an exempt capital gain [D. C. Code § 47-1557a(b)(11)].

2. Where a liquidating distribution in excess of earned surplus is made with respect to stock which is a capital asset, the policy of the D. C. Income Tax Act exempting capital gains from taxation requires that the shareholder's basis for the distributed property be equal to its fair market value.

The preceding discussion demonstrates that the evident scheme of the D. C. Income Tax Act is to treat a liquidating distribution as a dividend to the extent of the liquidating corporation's earned surplus, and as an amount received in exchange for the underlying stock as to any balance. The balance of the distribution should, therefore, qualify as an exempt capital gain under the D. C. Income Tax Act if the underlying stock was held for more than two years.

The D. C. Income Tax Act manifests an express policy of exempting gains arising from the sale or exchange of investment property which is

held for more than two years. Exemption of capital gains from the tax base is not a narrow loophole in the law, but represents a considered policy decision intended to encourage investment activities. In line with this policy, D. C. Code § 47-1557a(b)(11) provides that gross income does not include "(g)ains from the sale or exchange of any capital assets as defined in this subchapter," while D. C. Code § 47-1551c(1) defines a "capital asset" as any property, with certain exceptions not material, "held by the taxpayer for more than two years."

Where property is received by a taxpayer in a liquidating distribution in which a part of the distribution is treated as a payment in exchange for the underlying stock, a subsequent sale of the property received should not result in a taxable gain. This result is required by, and is consistent with, the policy expressed in the D. C. Income Tax Act of exempting capital gains. A contrary result would undermine this policy by treating the stockholder's capital gain on liquidation--which the D. C. Income Tax Act states is exempt--as merely being deferred until such time as the stockholder subsequently sells the property received.

The interrelationship between the policy of capital gain exemption and the problem of basis can best be illustrated by analyzing the facts of the present cases. At the time of the liquidation of Capitol, the Petitioners had a cost basis for their stock of $1,200, while Capitol's earned surplus was $99,000. As a result of the liquidation, Petitioners received property with a fair market value of $470,000, of which $99,800--the amount of

Capitol's earned surplus--was taxable as a dividend, $1,200 was a return to Petitioners of their original investment in the corporation, *i.e.*, their stock basis, and $369,000 was the appreciation in value of Capitol's assets ($470,000 total value less $101,000 total cost basis to Capitol). *Snow* v. *District of Columbia*, *supra*, at p. 526. As we have already demonstrated, this $369,000 appreciation in value represented a gain realized by the Petitioners from an exchange of their stock. Since they had held their stock in Capitol for more than two years, this gain was a capital gain and, as such, was not required to be included in their gross income. In other words, Petitioners' capital gain was exempt from tax.[4/]

Shortly after the liquidation of Capitol, the Petitioners sold the Chastleton Stock received by them upon the liquidation for $390,000, an amount equal to its fair market value at the time of the liquidation. At this point, in determining the D. C. income tax consequences of this sale, it becomes necessary to consider what was meant when it was concluded that Petitioners' $369,000 gain on liquidation was exempt. First, it is clear that the $390,000 received by Petitioners on the sale of the Chastleton Stock represented a portion of the $99,800 reported as a dividend on the liquidation, a portion of their $1,200 cost basis for the Capitol stock, and the $369,000 exempt capital gain. Second, it should be equally clear that if

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4/ "Income which is not includable in gross income obviously is 'wholly exempt'." *Hawaiian Trust Company Limited* v. *United States*, 291 F.2d 761, 772 (9th Cir. 1961).

Petitioners' sale of the Chastleton Stock for $390,000 results in a taxable gain of $369,000--as the District has contended in these cases--Petitioners' exempt capital gain is really not exempt at all. Instead, Petitioners have merely been accorded the privilege of postponing the recognition of their gain on liquidation until the later sale of the Chastleton Stock. Not only does this result do violence to the idea that Petitioners' gain on liquidation is exempt, but it also ignores the well-defined distinction between gain which is exempt and gain which is merely non-recognized. In Hawaiian Trust Company Limited v. United States, 291 F.2d 761, 773 (9th Cir. 1961), the Court stated:

> There is a valid distinction between "wholly exempt" income and income on which "no gain or loss is recognized". Wholly exempt income is never taxed. Nonrecognized gains are not taxed in the particular transaction that qualifies for nonrecognition treatment. They may be taxed, however, if the transaction fails to meet the nonrecognition requirements and may also be taxed at another time. In other words, they are not "wholly exempt" from the tax.

See also, Cotton States Fertilizer Co., 28 T.C. 1169 (1957).

The concept of a non-recognized gain is also found in other parts of the D. C. Income Tax Act.[5/] Therefore, it is not unreasonable to conclude

5/ See D.C. Code § 47-1583b which provides: "When in connection with the reorganization of a corporation, a taxpayer receives, in place of stock or securities owned by him, any stock or securities of the reorganized corporation, no gain or loss shall be deemed to occur from the exchange until the new stock or securities are sold or realized upon and the gain or loss is definitely ascertained, until which time the new stock or securities received shall be treated as taking the place of the stock or securities exchanged . . ."

that when Congress specified that capital gains should not be included in gross income, it intended that such income should be exempt. It did not intend merely that the recognition of that income would be deferred until such time as the property was sold, because if it had so intended it could easily have provided for this result as it did in other cases where that was its intention. It must, therefore, be concluded that since the clear intention of the D.C. Income Tax Act is to exempt capital gains, this policy will be frustrated if an immediate resale by the shareholder results in that same gain being subjected to tax. It was apparently in recognition of this fact that the District of Columbia conceded in its brief to the Court of Appeals in the celebrated "first" Oppenheimer case, that, in a case similar to this case, if "the property [received on liquidation] is sold immediately on receipt by the respondent [the stockholder of the distributing corporation] for its market value no gain will exist for District tax purposes."[6/] It seems to us that, in making this fundamental concession, the District has itself recognized that a fair market value basis must follow as a complement to an exempt capital gain.

It is, therefore, submitted that the liquidating distribution received by Petitioners from Capitol resulted in an exempt capital gain to the extent it exceeded Capitol's earned surplus, and that the only way, consistent with the underlying policy of the D.C. Income Tax Act, in which complete exemption may be given to such gains would be for this Court to hold that no taxable gain would be realized upon a subsequent sale of the assets received

6/ Brief for Petitioner, Docket No. 16,472, p. 10.

upon liquidation for an amount equal to the fair market value of those assets at the time of liquidation.

Under Federal income tax law, it is generally true that a stepped-up basis for property is not allowed in the case of a non-taxable transfer. The reason for this rule in Federal law is because all non-taxable transfers occur in situations where the taxpayer's realized gain on the transfer is not recognized, and the mechanism of a carry-over in basis is used to insure that the deferred gain will ultimately be subject to tax. However, this principle does not apply to the provisions of the D.C. Income Tax Act where, unlike Federal law, realized capital gains are exempt from tax.

Petitioners recognize that this Court's decision in the second Oppenheimer case, which held that a corporate liquidating distribution did not involve an exchange, is inconsistent with Petitioners' position in these cases. Moreover, the second Oppenheimer decision, on its facts as well as in its rationale, directly conflicts with the decision of a different panel of this Court in the Snow case. For the reasons set forth above, Petitioners believe that this Court's opinion in Snow is the better reasoned opinion and should be followed in these and other cases.

It is significant to note that there is no indication in Judge McGowan's opinion in Oppenheimer that his attention was directed to the relationship between the basis for property distributed on liquidation and the policy of the D.C. Income Tax Act exempting capital gains.[7/] The only

7/ In fact, the earlier decision in the Snow case was not even cited in the majority decision in Oppenheimer.

reason given by Judge McGowan in reaching his decision in second Oppenheimer was his belief that the Federal income treatment of a liquidation as an exchange was not controlling and his feeling that any other result would permit "a stockholder, simply by deciding to dissolve and liquidate the corporation . . . [to] acquire a depreciation base consisting of a book write-up of a value on which, very properly, no tax need be paid upon its receipt by the stockholder." 363 F.2d 709, 711. But as Petitioners have already demonstrated, the result which Judge McGowan refused to approve is precisely the result contemplated by the capital gains exemption contained in the D. C. Income Tax Act. Where the underlying stock has been held for more than two years so that the gain on the liquidation qualifies as an exempt capital gain, this exemption can be meaningful only if the distributed property obtains a fair market value basis for purposes of sale. Otherwise, the shareholder will, instead of enjoying an exemption required by the statute, be given only a temporary non-recognition, with the gain being taxable at some future time when he sells the distributed property.

II. IF PETITIONERS' COST BASIS FOR THE CHASTLETON STOCK IS DETERMINED BY REFERENCE TO CAPITOL'S COST BASIS, THEN PETITIONERS' HOLDING PERIOD SHOULD ALSO INCLUDE CAPITOL'S HOLDING PERIOD. ALTERNATIVELY, IF PETITIONERS' COST BASIS FOR THE CHASTLETON STOCK IS DETERMINED BY REFERENCE TO PETITIONERS' COST BASIS FOR THE STOCK OF CAPITOL HOTEL SURRENDERED THEREFOR, THEN PETITIONERS' HOLDING PERIOD SHOULD ALSO INCLUDE THEIR HOLDING PERIOD FOR THE CAPITOL HOTEL STOCK.

Petitioners have contended that they did not realize any taxable gain on their sale of the Chastleton Stock because the amount realized from the sale was not greater than their "cost" basis for the property sold. The District, on the other hand, imposed a tax on each Petitioner's pro rata share of a gain on sale computed in the following manner (Exhibit B attached to the Petitions, J.A. 9):

Total Sales Price	$390,000.00
Cost Basis	20,480.00
Gain on Sale	$369,520.00

The effect of the method employed by the District was to require each Petitioner to use as his "cost" basis for determining gain or loss on sale of the property received by him upon the liquidation of Capitol, the same basis which that property had in the hands of Capitol, the distributing corporation. In other words, the District required that Capitol's basis for the Chastleton Stock be carried over to its shareholders. Petitioners contend that if, in computing gain on sale of the property received by them upon the liquidation of Capitol, they are required to use Capitol's basis for such property, then they are also entitled to include Capitol's holding period in determining their own holding period for the Chastleton Stock.

This question of Petitioners' holding period becomes important because D.C. Code § 47-1557a(b)(11) exempts from gross income gains from the sale or exchange of "capital assets", while D.C. Code § 47-1551c(1) defines a "capital asset" as any property "held by the taxpayer for more than two years".

Petitioners contend that they satisfied the two year holding period requirement of D.C. Code 47-1551c(1), because as a fundamental, common law principle of income taxation, whenever a carry over in basis is required - *i.e.*, where the basis of property in the hands of a transferee of the property is determined by reference to the basis of such property in the hands of his transferor - a corresponding carry over in the holding period is also required. In other words, where the basis of property in the hands of a transferee is determined by reference to the basis of such property in the hands of the transferor, the period of time in which the transferee will be considered to have held the property must be deemed to include the period of time in which such property was held by the transferor. When Capitol's twelve year holding period for the Chastleton Stock is added to Petitioners' holding period, the two year holding period required to characterize the property as a capital asset will clearly be satisfied.[8/]

Petitioners admit that, unlike Federal income tax law, the D.C. Income Tax Act does not contain explicit statutory recognition of this principle. However, Petitioners contend that the combination of carry over in basis with a concomitant carry over in holding period is a basic and fundamental concept in the law of income taxation which subsists even in the absence of express statutory sanction. In *Helvering* v. *New York Trust Co.*, 292 U.S. 455 (1934), a father had transferred

8/ Capitol acquired the Chastleton Stock in 1948 (Stip. par. 11, J.A. 14).

corporate stock which he had held for more than two years to a trust for the benefit of his son. At a time when it had held the corporate stock for less than two years, the trust sold the stock at a profit. The Revenue Act of 1921, which was the law applicable to the sale, contained an inconsistency in that the donee (the trust) was required to use the donor's basis, but the statute was silent as to the use of the donor's holding period. This inconsistency resulted from a literal reading of the separate sections of the statute dealing with the subjects of basis and holding period. The Supreme Court held, despite the absence of statute, that the father's holding period also carried over to the trust, thereby permitting the stock to qualify for the lower rate applicable to capital assets held for more than two years. The Court reasoned that a contrary result would run counter to the very purpose of the capital gains rate reduction, which was intended to encourage the disposition of capital assets, and would penalize taxpayers making such sales. A departure from the strict terms of the statute was justified, the Court thought, in order to secure for the taxpayer the benefit intended to be conferred. Thus, the Court stated (292 U.S. 455, 467):

> While undoubtedly legally possible and within the power of Congress, the methods adopted and results attained by the Commissioner are so lacking in harmony as to suggest that the continuity required to be used to get the base was also intended for use in finding the rate [i.e., in determining the holding period]. No valid ground has been suggested for requiring tenures to be added for one purpose and forbidding the combination for the other. The legislative

> purpose to be served by the application of the lower rate upon capital gains [i.e., to lessen the deterrent effect of high rates on the disposition of capital assets] is directly opposed to the Commissioner's construction.

By this holding, the Supreme Court recognized the basic inconsistency in requiring a carry over in basis while not permitting a corresponding carry over in holding period.[9/] Similar recognition of this inconsistency is evidenced by the early administrative regulations which, again in the absence of statute, authorized a carry over of holding period in cases involving a carry over of basis following a tax-free exchange. Regs. 62, Art. 1651 (Revenue Act of 1921); Regs. 65, Art. 1651 (Revenue Act of 1924). See also I.T. 1765, II-2 C.B. 44.

The argument in favor of a tacking of holding period is further supported by this Court's decision in District of Columbia v. Lewis, 109 App. D.C. 353, 288 F. 2d 137 (1961), that the rulings and interpretations of Federal statutes should be applied to cognate provisions of the D.C. Income Tax Act. In fact, in the Lewis case, this Court went so far as to require that language contained in a Federal statute, not found in a cognate provision of the D.C. Income Tax Act, be written into the latter as if it had originally appeared therein. We submit that the principle of the Lewis case is applicable here.

9/ In so holding, the Court refused to follow an earlier decision of this Court, Shoenberg v. Burnet, 60 App. D.C. 381, 55 F. 2d 543 (1931), which, on identical facts, had refused to permit a tacking of holding period.

Since the enactment of Section 208(a)(8) of the Revenue Act of 1926, 44 Stat. 9, Federal income tax law has contained a provision substantially identical to that now found in Section 1223(2) of the Internal Revenue Code of 1954, which provides as follows:

> In determining the period for which the taxpayer has held property however acquired there shall be included the period for which such property was held by any other person, if under this chapter such property has, for the purpose of determining gain or loss from a sale or exchange, the same basis in whole or in part in his hands as it would have in the hands of such other person.

The legislative history of this provision indicates that Congress did not regard the predecessor of Section 1223(2) as working a basic, fundamental change in the law. Instead, Congress thought that it was merely making a clarifying amendment which confirmed a prior administrative regulation reaching the same result. H. Rep. No. 1, 69th Cong., 1st Sess. p. 6, 1939-1 C. B. (Part 2) 319. Prior to the enactment of the language now found in Section 1223(2) of the Internal Revenue Code of 1954, the Treasury had, by administrative regulation, reached the same result which was later codified in the Revenue Act of 1926. Regs. 62, Art. 1651 (Revenue Act of 1921); Regs. 65, Art. 1651 (Revenue Act of 1924). See also, I. T. 1765, II-2 C. B. 44. The only basis for these administrative regulations at the time of their promulgation was the fundamental common law principle of income taxation that a carry over in basis <u>and</u> a carry over of holding period are necessary concomitants, so that, conceptually,

if one is present by legislative mandate the other must also be present by necessary implication.

We submit that the language of D.C. Code § 47-1557c(1), which defines the term "capital assets," should be construed as necessarily encompassing this concept of "tacking" of holding period. Specifically, the phrase "held by the taxpayer", contained therein, should be interpreted, under the authority of District of Columbia v. Lewis, supra, as including the long-standing provisions of the Federal law now found in Section 1223(2) of the Internal Revenue Code of 1954. In the alternative, the phrase "held by the taxpayer" should be construed in the light of the interpretation given to that term in the Treasury regulations cited above which, despite the absence of express statutory authorization, but as a fundamental principle of income taxation, permitted a "tacking" of holding period where a carry over in basis was required.

The Tax Court's opinion sustaining the District's assessments in these cases will not, in our opinion, withstand a reasoned and logical analysis. On the one hand, the Tax Court held, in rejecting the Petitioners' argument for a fair market value basis, that the Petitioners' basis for the Chastleton Stock "was not the unrealized, but the realized value, that is to say, $20,480.00" (J.A. 21), which, of course, was the same basis which the Chastleton Stock had in the hands of Capitol. On the other hand, in rejecting Petitioners' argument for a tacking of holding period, the Tax Court stated (J.A. 31-32):

> The Court did not hold in deciding these cases on remand that the basis of the Capitol Hotel Enterprises, Inc. should be the basis of the stockholders. The question of capital gains or Capitol Hotel Enterprises, Inc. basis was not involved. All that was decided was that the basis of the stockholders in determining gain was the realized value of the asset they received from the corporation and then sold by them. The realized value happened to be the same as the basis of the Capitol Hotel Enterprises, Inc. but the case did not turn on that fact.

The Tax Court's decisions on the basis and holding period questions are obviously conflicting and internally inconsistent. Capitol's original cost basis for the Chastleton Stock was $20,480. This amount is presumably what the Tax Court referred to as Petitioners' "realized value" for the Chastleton Stock after it was distributed in connection with Capitol's liquidation. And the Tax Court's original opinion certainly states that this realized value, "that is to say, $20,480.00" (J.A. 21), was Petitioners' basis for the Chastleton Stock received upon the liquidation. If this is so--and the Tax Court's subsequent Memorandum also recognizes that "the basis of the stockholders [Petitioners] in determining gain was the realized value [$20,480] of the asset they received" (J.A. 32)--then we are unable to understand the Tax Court's statement, contained in the immediately preceding sentence of its Memorandum, that it "did not hold...that the basis of...Capitol...should be the basis of the stockholders" (J.A. 31-32). Unfortunately, after reading the Tax Court's original opinion and its later Memorandum, Petitioners are unable to construct any consistent, logical pattern to serve as a guideline for this case or other cases like it.

It seems to us that if this Court declines to accept the argument favoring a fair market value basis, then there are only two other alternative theories for determining the basis to the stockholders of property received as a liquidating distribution:

(1) First, it may be determined that the corporation's basis for the assets (the Tax Court's concept of "realized value") carries over to the stockholders after the liquidation. This would be an example of a concept which, for Federal income tax purposes, is referred to as a "transferred basis," that is, the basis of the property in the hands of a transferee is determined by reference to the basis of such property in the hands of the transferor. This appears to be the position taken by the District in assessing the tax in these cases and also appears to be the position approved by the Tax Court in these cases. On this theory, Helvering v. New York Trust Co., supra, would directly support a tacking of holding period.

(2) The second alternative would be that the shareholders' basis for the assets received on liquidation is equal to the cost basis for the stock surrendered on the liquidation plus the amount of income, if any, recognized in connection with the dividend resulting from the liquidation. This alternative, involving a so-called "substituted basis." is predicated on the theory that the liquidation of the corporation and the distribution of the assets to the shareholders involve merely a change in the form, and not the substance, of ownership of the assets and that, accordingly,

the assets distributed in liquidation should be regarded as taking the place of the corporate stock previously owned by the shareholders. Support for this position may be found in the Tax Court's decision in the second _Oppenheimer_ case, _Oppenheimer_ v. _District of Columbia_, DC CT ¶200-047, affirmed, ___ App. D.C. ___, 363 F.2d 708 (1966).

Regardless of the method used for determining Petitioners' basis for the Chastleton Stock, Petitioners should be treated as having held the Chastleton Stock for more than two years, either by adding to their holding period the twelve year period in which the Chastleton Stock was held by Capitol (on the theory of a transferred basis) or by adding to their holding period the twelve year period in which they held their common stock in Capitol (on the theory of a substituted basis). Under either method, the Chastleton Stock qualified as a capital asset in Petitioners' hands and the gain on the sale was an exempt capital gain.

III. AS AN ALTERNATIVE, THE DISTRICT OF COLUMBIA ERRED IN FAILING TO ALLOCATE PETITIONERS' COST BASIS FOR THE CHASTLETON STOCK ON THE BASIS OF THE AMOUNT OF THE DISTRIBUTION TREATED AS A TAXABLE DIVIDEND IN PROPORTION TO THE RESPECTIVE FAIR MARKET VALUES OF THE DISTRIBUTED PROPERTY.

In computing gain on the sale of the Chastleton Stock, the District of Columbia reduced each Petitioner's share of the total amount realized on the sale by his pro rata share of Capitol's cost basis for the Chastleton Stock. The District of Columbia ignored the fact that at the same time that the Petitioners were being required to report gain on the sale of the

Chastleton Stock, they were also being required to report, as a dividend, their respective pro rata shares of Capitol's earned surplus.

Petitioners admit that they were properly required to report as a dividend their respective pro rata shares of Capitol's earned surplus. Petitioners contend, however, in the event the preceding arguments are rejected, that in any event they are entitled to use as the basis for the Chastleton Stock distributed to them an amount equal to that portion of Capitol's earned surplus which the fair market value of the Chastleton Stock bore to the fair market value of all assets distributed by Capitol on liquidation.

It is axiomatic that Capitol's earned surplus of $99,821.30 did not constitute a physically identifiable fund, but represented only a bookkeeping entry reflecting the amount by which Capitol's assets exceeded the sum of its liabilities and paid-in capital. Therefore, when Capitol distributed its assets in liquidation the dividend received by each Petitioner was not represented by any specific property distributed by Capitol. Instead, the shareholders received Chastleton stock having a fair market value of $390,000 and other unrelated assets having a fair market value of $80,541.30. Because Capitol had earned surplus and because the value of the property distributed was at least equal to the amount of Capitol's earned surplus, Petitioners received a dividend equal to their respective pro rata shares of such earned surplus. In addition, there was returned to Petitioners their respective pro rata shares of their original contribution to Capitol's capital.

The District of Columbia apparently admits that, as a minimum, the aggregate cost basis to the shareholders of Capitol of the assets distributed on liquidation was equal to the sum of Capitol's earned surplus of $99,921.30 and the original capital investment of $1,200 or $101,021.30. The parties differ, however, in the manner in which the amount of $101,021.30 should be allocated between the Chastleton Stock and the other unrelated assets. The District of Columbia made this allocation on the basis of the book value of the assets involved. Petitioners, on the other hand, contend that the amount of $101,021.30 should be allocated among the assets distributed on the basis of their respective fair market values.

It is well established under the Federal income tax law that where a mixed aggregate of assets is required at one time, the total cost basis is allocated among all of such assets on the basis of their relative fair market values at the time of acquisition. C. D. Johnson Lumber Corporation, 12 T.C. 348 (1949); Clifford Hemphill, 25 B.T.A. 1351 (1932); Frances E. Clark, 28 B.T.A. 1225 (1933), aff'd 77 F.2d 89 (3d Cir. 1935). Similarly, in a number of instances where the Federal income tax statutes require that an allocation of basis be made among several assets, but do not specify the method of allocation, the implementing regulations promulgated by the Treasury Department specify an allocation based upon fair market value. See, for example, Treas. Regs. § 1.307-1(a) (distribution of stock rights); § 1.334-1(c) (corporate liquidation); § 1.334-2 (one-month corporate liquidation); § 1.358-2 (distribution in corporate reorganization).

In view of the absence of contrary authority, Petitioners submit that the only proper method of allocation in these cases is on the basis of fair market values. *Cf.* *District of Columbia* v. *Lewis*, *supra*.

CONCLUSION

For the reasons set forth above, it is respectfully urged that the relief requested herein be granted, that the judgments of the Tax Court be reversed and that this Court enter judgment in each case for the refund sought, or for such other amount as this Court shall deem proper, together with interest and costs allowed by law.

Respectfully submitted,

____
Albert E. Arent

____
Joel N. Simon

Attorneys for Petitioners
1815 H Street, N. W.
Washington, D. C. 20006

CERTIFICATE OF SERVICE

It is hereby certified that a copy of the foregoing Brief for Petitioners was mailed first-class, postage prepaid, to the office of the Corporation Counsel, D.C., this ______day of May, 1967.

____
Joel N. Simon

APPENDIX

STATUTES INVOLVED

District of Columbia Income and Franchise Tax Act of 1947, Act of July 16, 1947, 61 Stat. 331:

D. C. Code § 47-1551c provides:

* * *

(l) The words "capital assets" mean any property, whether real or personal, tangible or intangible, held by the taxpayer for more than two years (whether or not connected with his trade or business), but do not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the end of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business.

(m) the word "dividend" means any distribution made by a corporation (domestic or foreign) to its stockholders or members, out of its earnings, profits, or surplus (other than paid-in surplus), whenever earned by the corporation and whether made in cash or any other property (other than stock of the same class in the corporation if the recipient of such stock dividend has neither received nor exercised an option to receive such dividend in cash or in property other than stock instead of stock) and whether distributed prior to, during, upon, or after liquidation or dissolution of the corporation: Provided, however, That in the case of any dividend which is distributed other than in cash or stock in the same class in the corporation and not exempted from tax under this sub-chapter, the basis of tax to the recipient thereof shall be the market value of such property at the time of such distribution: And provided, however, That the word "dividend" shall not include any dividend paid by a mutual life insurance company to its shareholders.

* * *

D. C. Code § 47-1557a provides:

Gross income and exclusions therefrom.

(a) The words "gross income" include gains, profits, and income derived from salaries, wages, or compensation for personal services of whatever kind and in whatever form paid, including salaries, wages, and compensation paid by the United States to its officers and employees to the extent the same is not exempt under this subchapter, or income derived from any trade or business or sales or dealings in property, whether real or personal, other than capital assets as defined in this subchapter, growing out of the ownership, or sale of, or interest in, such property; also from rent, royalties, interest, dividends, securities, or transactions of any trade or business carried on for gain or profit, or gains or profits, and income derived from any source whatever.

(b) The words "gross income" shall not include the following:

* * *

(11) Capital Gains. -- Gains from the sale or exchange of any capital assets as defined in this subchapter.

* * *

D. C. Code § 47-1557b provides:

Deductions.

(a) Deductions allowed.—The following deductions shall be allowed from gross income in computing net income:

* * *

(4) Losses. -- Losses sustained during the taxable year and not compensated for by insurance or otherwise --

* * *

(B) if incurred in any transaction entered into for the production or collection of income subject to tax under this subchapter, or for the management, conservation, or maintenance of property held for the production of income subject to tax under this subchapter, though not connected with any trade or business;

* * *

(b) Deductions not allowed. —In computing net income, no deduction shall be allowed in any case for --

* * *

(6) Capital losses. — Losses from the sale or exchange of any capital asset as defined in this subchapter.

* * *

D. C. Code § 47-1583 provides:

Basis for determining gain or loss.

The basis for determining the gain or loss from the sale, exchange, or other disposition of property shall be the cost of such property, . . .

* * *

D. C. Code § 47-1583a provides:

Gain or loss from sale or other disposition of property.

(a) Computation of gain or loss. --The gain or loss, as the case may be, from the sale or other disposition of property shall be the difference between (a) the amount realized from such sale or other disposition of the property and (b) the basis as defined in section 47-1583.

(b) Amount realized. -- The amount realized from the sale or exchange of property shall be its selling price, . . .

* * *

D.C. Code §47-1583c provides:

Basis for dividends paid in property.

Where any property other than money is paid by a corporation as a dividend, the base to the recipient thereof shall be the market value of such property at the time of its distribution by such corporation.

JOINT APPENDIX

DISTRICT OF COLUMBIA TAX COURT

JOHN H. VERKOUTEREN, Petitioner, vs. DISTRICT OF COLUMBIA, Respondent.	)	DOCKET NO. 1897
HERMAN OSHINSKY, Petitioner, vs. DISTRICT OF COLUMBIA, Respondent.	)	DOCKET NO. 1898
MARY OSHINSKY, WILLIAM OSHINSKY and CLARA SENNET, Executors of the Estate of Charles Oshinsky, Petitioners, vs. DISTRICT OF COLUMBIA, Respondent.	)	DOCKET NO. 1899
WILLIAM OSHINSKY, Petitioner, vs. DISTRICT OF COLUMBIA, Respondent.	)	DOCKET NO. 1900
HERMAN FENICHEL, Petitioner, vs. DISTRICT OF COLUMBIA, Respondent.	)	DOCKET NO. 1901
BERNARD MARGOLIUS and LILYAN MARGOLIUS, Petitioners vs. DISTRICT OF COLUMBIA, Respondent.	)	DOCKET NO. 1902

INDEX

[Filed August 13, 1963]

PETITION

The above-named Petitioner appeals from an assessment of taxes against him and avers as follows:

1. The Petitioner, John H. Verkouteren, is an individual residing at 1343 H Street, N. W., Washington, D. C.

2. The Statement of Taxes Due, a copy of which is attached hereto and marked Exhibit A, was dated May 17, 1963. The tax, together with interest thereon, was paid by Petitioner on June 12, 1963. The Notice of Deficiency, dated December 31, 1962, together with a copy of the audit report, is attached hereto as Exhibit B.

3. The tax in controversy is in respect of income tax for the calendar year 1960 in the amount of $4,686.28, and interest thereon in the amount of $609.22.

4. The assessment of tax is based upon the following error: Respondent erred in determining that Petitioner should have included in gross income for the calendar year 1960 gain upon the sale of shares of capital stock of Chastleton Hotel, Inc.

5. The facts upon which Petitioner relies as the basis of this proceeding are as follows:

(a) The Petitioner, prior to January 29, 1960, was the owner of 100 shares of the common stock of Capitol Hotel Enterprises, Inc., a

Delaware corporation (hereinafter referred to as the "Corporation"), which he acquired upon the organization of the Corporation in 1948. From the date of its incorporation until January 29, 1960, the business of the Corporation consisted of the ownership and management of investment properties situated in the District of Columbia.

(b) On January 29, 1960, the Corporation was dissolved upon the filing of a Certificate of Dissolution with the Office of the Secretary of State in Delaware. Immediately prior to such dissolution, the Corporation's assets, liabilities, and net worth were as set forth on the balance sheet attached hereto as Exhibit C and made a part hereof. Included among the assets of the Corporation were 200 shares of Preferred Stock and 480 shares of Common Stock of Chastleton Hotel, Inc., a Delaware corporation (hereinafter referred to as "Chastleton"), which the Corporation had purchased in 1948 for $20,000.00 and $480.00, respectively. Immediately prior to dissolution, the shares of capital stock of Chastleton owned by the Corporation had a fair market value of not less than $390,000.00, and the assets of the Corporation other than Chastleton capital stock had a fair market value of not less than their respective book values.

(c) On January 29, 1960, upon dissolution of the Corporation, Petitioner received, in complete cancellation and redemption of the common stock of the Corporation owned by him, 40 shares of Preferred

Stock and 96 shares of Common Stock of Chastleton, and a proportionate interest in the other assets of the Corporation.

(d) On February 1, 1960, Petitioner sold the 40 shares of Chastleton Preferred Stock and the 96 shares of Chastleton Common Stock for a total aggregate of $78,000.00, payable $59,800.00 in cash and the balance by a one year promissory note of the purchaser payable February 1, 1961, with interest at 6 percent per annum. This sale of Petitioner's Chastleton capital stock was made in conjunction with the sale, made by all former stockholders of the Corporation, of all of the shares of Chastleton capital stock formerly owned by the Corporation, i.e., 200 shares of Preferred Stock and 480 shares of Common Stock, to a single purchaser for a total purchase price of all such shares of Chastleton capital stock of $390,000.

WHEREFORE, Petitioner prays that this Court may hear this case and:

1. Determine that the deficiency asserted by the Respondent for the calendar year 1960 is erroneous.

2. Determine that Petitioner is entitled to a refund of the tax and interest paid pursuant to the Statement of Tax Due attached hereto as Exhibit A.

3. Grant any further and additional relief to which the Petitioner is entitled.

/s/ Albert E. Arent

/s/ Joel N. Simon

Attorneys for Petitioner
1000 Federal Bar Building
Washington 6, D. C.

John H. Verkouteren, being duly sworn, states that he is the Petitioner above named, that he has read the foregoing Petition and is familiar with the statements contained therein; and that he verily believes that the statements contained therein are true.

/s/ John H. Verkouteren

[JURAT dated August 12, 1963]

[Identical Petitions, with the exception of numerical differences, were filed in the Tax Court in the other consolidated cases, Docket Nos. 1898-1902, on August 13, 1963.]

EXHIBIT A

GOVERNMENT OF THE DISTRICT OF COLUMBIA
FINANCE OFFICE • Revenue Di[illegible]ion

INCOME AN[illegible] FRANCH[illegible]SE TAX

COPY 1A – TAXPAYER'S COPY

TYPE TAX	ACCOUNT NUMBER	REF.	TYPE TAX	TAX YEAR	DATE	
I - I[illegible]ividual Income D - Declaration Payment N - Corporation J - Unincorporated Business F - Fiduciary E - Employer Withholding						

NAME AND ADDRESS	TOTAL TAX DOLLARS	TOTAL TAX CTS.	CREDIT DOLLARS	CREDIT CTS.	INTEREST TO	PAYMENT DUE DOLLARS	PAYMENT DUE CTS.
Paid 6/.r/63.	ck # 3370	hat	Saci r Tr				

Interest on payment due at the rate of ½ of 1% per month or portion thereof must be added if not paid on or before the interest date shown on this bill. Late filing penalty is computed at 5% per month or portion thereof (maximum 25%), except type tax E which is a flat 25%.

Make check payable to D. C. TREASURER. Send check or money order to FINANCE OFFICE, REVENUE DIVISION, Municipal Center, Washington 1, D. C.

FPr 56 (9/60) Your cancelled check is your receipt.

Interest at rate of ½ of 1% per month or portion thereof
from to

TOTAL PAYMENT DUE ⟶

KEEP THIS COPY

EXHIBIT B

GOVERNMENT OF THE DISTRICT OF COLUMBIA
DEPARTMENT OF GENERAL ADMINISTRATION

FINANCE OFFICE:
REVENUE DIVISION

REPLY TO:
INCOME AND FRANCHISE TAX SECTION
ROOM 2034, MUNICIPAL CENTER
300 INDIANA AVENUE, N. W.
WASHINGTON 1, D. C.

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

December 31, 1962

Mr. John H. Verkouteren
1343 H Street, N. W.
Washington, D. C.

Re: No. 3294275(WRE)

Dear Sir:

The examination by this office of your Individual Income Tax return(s) for the year(s) ended December 31, 1960, indicates that the adjustment of your tax liability, as shown in the accompanying Report(s) of D. C. Individual Income Tax Audit Changes, is warranted.

IF YOU AGREE to the adjustment(s), as shown in the report(s), the enclosed form of waiver should be executed and forwarded to this office promptly. Action will then be taken as indicated on line 13 or 14 of the report(s), whichever is applicable.

IF YOU DO NOT AGREE to the adjustment(s), you may file a protest with this office, within thirty (30) days from the date of this letter, stating the grounds for your exceptions. Careful consideration will be given to such protest and, if you so request, an opportunity for a hearing in this office will be granted to you prior to final determination.

Should you fail to file either the enclosed waiver form or a written protest with this office within the thirty (30) day period, final determination of your tax liability will be made in accordance with the enclosed report(s).

Yours very truly,

Ben A. Barsky

Ben A. Barsky
Supervisory Tax Auditor
Income and Franchise Tax Section

Enclosures:
Waiver Form
Statement(s)

FR-181 (Rev. 8-61)

Finance Office
Revenue Division

GOVERNMENT OF THE DISTRICT OF COLUMBIA
REPORT OF D. C. INDIVIDUAL INCOME TAX AUDIT CHANGES

Name and Address of Taxpayer(s)	Return Number	Date of Report
John H. VerKouteren 1343 H Street NW. Washington D.C.	3294275	Nov 21, 1962
	Year Ended	**Tax Auditor**
	12/31/60	W. R. Edelin

1. Taxable income shown on return or as previously adjusted		$ 23,573.57
2. ADD: Additional income or unallowable deductions:		
(1) Dividend: Capitol Hotel Enterprises	$ 19,964.26	
(2) Gain on sale of Charleston Hotel Stock	73,904.00	
		93,868.26
3. Total of lines 1 and 2		$ 117,441.83
4. LESS: Decrease in income or additional deductions:		
	$	
5. Revised taxable income		$ 117,441.83
6. Revised tax liability		$ 5497.09
7. LESS: Total tax shown on return or as previously adjusted		810.81
8. Deficiency in tax		$ 4686.28
9. ADD: Penalty, if any		
10. Total of lines 8 and 9		$ 4686.28

Computation of Corrected Balance Due or of Net Overpayment

11. Revised tax liability and penalty, if any (total of lines 6 and 9)		$ 5497.09
12. LESS: Total tax paid A. Tax withheld	$	
B. Payments on estimated tax	830.20	
C. With return		
D. Sum of items A through C	830.20	
E. Deduct previous refunds and/or credits	19.39	810.81
13. Balance due (Line 11 less line 12) Upon receipt of signed waiver, a bill will be mailed to you for this amount with interest thereon as provided by Law.		$ 4686.28
14. Net overpayment (Line 12 less line 11) Upon receipt of signed waiver, a refund will be authorized for this amount		$

See other side for explanation of adjustments

Form FR-115 (4-61) LC-7

(1) See attached statement:

Your share $\frac{100}{500}$ of \$99,821.30 = \$19,964.26

(2) Your share $\frac{100}{500}$ of \$369520.00 = \$73,904.00

Capitol Hotel Enterprises

Distribution in Liquidation

Distribution:

Notes and accrued Interest: Carlyle Realty Co	$80,541.30
Chastleton Hotel Stock	20,480.00
	$101,021.30
Less: Return of Capital	1200.00
Total Liquidating dividend	$99,821.30

Gain on sale of Chastleton Hotel Stock:

Selling Price	$390,000.00
Cost basis	20,480.00
Gain on sale	$369,520.00

Inasmuch as this stock was held for less than two years this gain is fully taxable

THE WORD "DIVIDEND" AS DEFINED IN TITLE I, SECTION 4(m), DISTRICT OF COLUMBIA INCOME AND FRANCHISE TAX ACT OF 1947, [illegible] [illegible]ES THAT TYPE OF DISTRIBUTION KNOWN AS "LIQUIDATING DIVIDENDS" AND THE TAXABILITY THEREOF IS PROVIDED IN TITLE III, SECTION 2 OF THE ACT.

EXHIBIT C

CAPITOL HOTEL ENTERPRISES, INC.

BALANCE SHEET
AS OF JANUARY 29, 1960
(Immediately prior to Distribution)

ASSETS

	80541.30
Notes Receivable - Carlyle Realty Co.	$ 76,603.80
Accrued Interest Receivable - Carlyle Realty Co.	3,937.50
Investment in Chastleton Hotel, Inc.	
200 shares, Preferred Stock	20,000.00
480 shares, Common Stock	480.00
Total Assets	$ 101,021.30

LIABILITIES AND NET WORTH

Liabilities	None
Net Worth:	
Common Stock, 500 shares issued and outstanding	$ 1,200.00
Earned Surplus	99,821.30
Total Liabilities and Net Worth	$ 101,021.30

[Filed November 14, 1963]

STIPULATION OF FACTS

It is hereby stipulated by and between the undersigned, as attorneys for the parties in the above-captioned cases, that the following facts shall be deemed and taken to be true for all purposes of these proceedings; provided, that each party reserves the right to introduce such other and further evidence as is not inconsistent with any of the facts set forth herein; and provided, further, that each party reserves the right to object to any factual statement contained herein on the grounds that it is irrelevant or immaterial to the issues raised by these proceedings:

1. Plaintiff, John H. Verkouteren, is an individual residing at 1343 H Street, N. W., Washington, D. C.

2. Plaintiff, Herman Oshinsky, is an individual residing at 8201 16th Street, Silver Spring, Maryland. During the calendar year 1960, plaintiff resided at 1601 Holly Street, N. W., Washington, D. C.

3. Plaintiff, Charles Oshinsky, is an individual residing at 4201 Cathedral Avenue, N. W., Washington, D. C.

4. Plaintiff, William Oshinsky, is an individual residing at 1437 Iris Street, N. W., Washington, D. C.

5. Plaintiff, Herman Fenichel, is an individual residing at 6101 16th Street, N. W., Washington, D. C.

6. Plaintiffs, Bernard Margolius and Lilyan Margolius, are individuals residing at 1561 Locust Road, N. W., Washington, D. C. Plaintiff, Lilyan Margolius, the wife of Bernard Margolius, is a party hereto only because a joint return was filed for the calendar year 1960. All references herein will be to plaintiff Bernard Margolius.

7. Each of the plaintiffs, on or before April 15, 1961, filed his respective District of Columbia Individual Income Tax Return for the calendar year 1960 on a cash basis with the Finance Office, District of Columbia, reporting thereon net taxable income and a tax liability in the following amounts:

Plaintiff	Reported on 1960 Return: Net Taxable Income	Tax Liability
John H. Verkouteren	$ 23,573.57	$ 810.81
Herman Oshinsky	19,887.41	645.50
Charles Oshinsky	15,753.33	480.13
William Oshinsky	15,153.73	456.15
Herman Fenichel	22,530.57	763.88
Bernard Margolius	84,327.65	3,841.38

The amounts of plaintiffs' respective tax liabilities, as reported on the 1960 returns, were duly assessed and paid to the District of Columbia.

8. After an examination of plaintiffs' D. C. Individual Income Tax Returns for the calendar year 1960, the net income tax liability of each Plaintiff for such year was revised in accordance with a revenue agent's report, dated November 21, 1962, transmitted to each plaintiff by a letter of the Supervisory Tax Auditor, Income and Franchise Tax Section, D. C. Finance Office, dated December 31, 1962. The income tax deficiencies for the year 1960, as shown in the revenue agent's report were duly assessed and paid, together with interest thereon, as follows:

Plaintiff	Deficiency Per R.A.R.	Date Assessed	Date Paid	Int. Paid on Deficiency
John H. Verkouteren	$4,686.28	May 17, 1963	June 12, 1963	$609.22
Herman Oshinsky	1,538.34	May 17, 1963	June 15, 1963	199.98
Charles Oshinsky	1,497.01	May 17, 1963	June 12, 1963	194.61
William Oshinsky	1,503.92	May 17, 1963	June 10, 1963	195.51
Herman Fenichel	3,116.59	May 17, 1963	June 10, 1963	405.16
Bernard Margolius	1,564.47	May 17, 1963	June 12, 1963	203.38

9. The adjustments made by the revenue agent in his report of November 21, 1962 to the net income and tax liability reported by each plaintiff on his respective 1960 tax return consisted of adding to the reported taxable income of each plaintiff the amount of a dividend from Capitol Hotel Enterprises, Inc., a Delaware corporation (hereinafter referred to as "Capitol") and an amount of gain on the sale of capital

stock of Chastleton Hotel, Inc., a Delaware corporation (hereinafter referred to as "Chastleton"), as follows:

Plaintiff	Amount of Adjustment: Dividend from Capitol	Amount of Adjustment: Gain on Sale of Chastleton Stock
John H. Verkouteren	$19,964.26	$73,904.00
Herman Oshinsky	6,654.76	24,634.67
Charles Oshinsky	6,654.75	24,634.67
William Oshinsky*/	6,654.75	24,634.67
Herman Fenichel	13,309.50	49,269.33
Bernard Margolius	6,654.75	24,634.67

The Plaintiffs do not challenge the correctness of the adjustment made by the revenue agent with respect to the amount treated as a dividend from Capitol. Each Plaintiff admits that the amount set forth opposite his name in the above column labeled "Dividend from Capitol" is properly to be treated as a dividend for District of Columbia income tax purposes.

10. Capitol was organized in 1948. From the date of its incorporation until January 29, 1960, the business of Capitol consisted of the ownership and management of investment properties situated in the District of Columbia. Prior to January 29, 1960, each of the plaintiffs was the owner of shares of the common stock of Capitol which he had acquired in and held since 1948, as follows:

Plaintiff	Number of Shares Owned
John H. Verkouteren	100
Herman Oshinsky	33-1/3
Charles Oshinsky	33-1/3
William Oshinsky	33-1/3
Herman Fenichel	66-2/3
Bernard Margolius	33-1/3

*/ With respect to plaintiff, William Oshinsky, the revenue agent's report also disallowed a medical expense deduction in the amount of $258.29. Plaintiff, William Oshinsky, does not challenge the correctness of this adjustment.

As of January 29, 1960, there were a total of 500 shares of common stock of Capitol issued and outstanding, and such common stock constituted the only authorized class of capital stock of Capitol.

11. On January 29, 1960, Capitol was dissolved upon the filing of a Certificate of Dissolution with the Office of the Secretary of State in Delaware. Immediately prior to such dissolution, Capitol's assets, liabilities, and net worth were as set forth on the balance sheet attached to this Stipulation of Facts as Exhibit A and made a part hereof to the same extent as if set forth herein in full. Included among the assets of Capitol were 200 shares of Preferred Stock and 480 shares of Common Stock of Chastleton which Capitol had purchased in 1948 for $20,000 and $480.00, respectively. Immediately prior to dissolution, the shares of capital stock of Chastleton owned by Capitol had a fair market value of not less than $390,000.00, and the assets of Capitol other than the Chastleton capital stock had a fair market value of not less than their respective book values.

12. On January 29, 1960, upon dissolution of Capitol, each of the Plaintiffs received, in complete cancellation and redemption of the common stock of Capitol owned by him, a proportionate interest in all of the assets of Capitol, including the following number of shares of the Preferred Stock and Common Stock of Chastleton:

	Shares of Chastleton Capital Stock Received	
Plaintiff	Preferred	Common
John H. Verkouteren	40	96
Herman Oshinsky	13-1/3	32
Charles Oshinsky	13-1/3	32
William Oshinsky	13-1/3	32
Herman Fenichel	26-2/3	64
Bernard Margolius	13-1/3	32

13. On February 1, 1960, each of the Plaintiffs sold the shares of Preferred Stock and Common Stock of Chastleton received by him upon the dissolution of Capitol for the amount set forth below. The purchase

price was paid to each of the Plaintiffs partly in cash and the balance by a one-year promissory note of the purchaser, payable February 1, 1961, with interest at 6 percent per annum, as follows:

Plaintiff	Amount Paid to Each Plaintiff: Total	In Cash	By Promissory Note
John H. Verkouteren	$78,000.00	$59,800.00	$18,200.00
Herman Oshinsky	26,000.00	19,933.33	6,066.67
Charles Oshinsky	26,000.00	19,933.33	6,066.67
William Oshinsky	26,000.00	19,933.33	6,066.67
Herman Fenichel	52,000.00	39,866.66	12,133.34
Bernard Margolius	26,000.00	19,933.33	6,066.67

This sale of Plaintiffs' capital stock of Chastleton was made in conjunction with the sale, made by all former stockholders of Capitol of all of the shares of Chastleton capital stock formerly owned by Capitol, i.e., 200 shares of Preferred Stock and 480 shares of Common Stock, to a single purchaser for a total purchase price for all such shares of Chastleton capital stock of $390,000.

IN WITNESS WHEREOF, this Stipulation of Facts has been executed by the undersigned this 8th day of November 1963.

Attorneys for the District of Columbia

/s/ Chester H. Gray
Corporation Counsel, D. C.

/s/ Henry E. Wixon
Assistant Corporation Counsel, D.C.

Attorneys for Plaintiffs

/s/ Albert E. Arent

/s/ Joel N. Simon

EXHIBIT A

CAPITOL HOTEL ENTERPRISES, INC.

BALANCE SHEET
AS OF JANUARY 29, 1960
(Immediately prior to Dissolution)

ASSETS

Notes Receivable - Carlyle Realty Co.	$ 76,603.80
Accrued Interest Receivable - Carlyle Realty Co.	3,937.50
Investment in Chastleton Hotel, Inc.	
200 shares, Preferred Stock	20,000.00
480 shares, Common Stock	480.00
Total Assets	$101,021.30

LIABILITIES AND NET WORTH

Liabilities	None
Net Worth:	
Common Stock, 500 shares issued and outstanding	$ 1,200.00
Earned Surplus	99,821.30
Total Liabilities and Net Worth	$101,021.30

[Filed November 10, 1966]

FINDINGS OF FACT AND OPINION ON REMAND

This Court held that the sale of certain capital stock of Chastleton Hotel, Inc., hereinafter called "Chastleton", formerly owned by Capitol Hotel Enterprises, Inc., hereinafter called "Capitol", was constructively sold for tax purposes by that corporation, and not by its stockholders. The United States Court of Appeals for the District of Columbia Circuit held on review that the holding by this Court was erroneous, and that the sale was made by the stockholders after the stock had been distributed to them, and remanded the case with instructions that this Court decide the question of the taxability of the stockholders with that premise. *Verkouteren* v. *District of Columbia*, 120 U.S. App. D.C. 361, 346 F.2d 842, 93 W.L.R. 991.

Findings of Fact

All of the facts have been stipulated by the parties and, as stipulated, are found by the Court.

Opinion

The issue presented in all of the above cases is the same. It involves the application of four sections of the Code, namely Sections 47-1551c(l), 47-1551c(m), 47-1557a and 47-1557b(11), District of Columbia Code, 1961 Edition.

Section 47-1551c(l) defines the words "capital assets" as "any property * * * held by the taxpayer for more than two years".

Section 47-1551c(m), as far as pertinent, is in the language following:

> "(m) The word 'dividend' means any distribution made by a corporation (domestic or foreign) to its stockholders or members, out of its earnings, profits, or surplus (other than paid-in surplus), whenever earned by the corporation and whether made in cash or any other property (other than stock of the same class in the corporation if the recipient of such stock dividend has neither received nor exercised an option to receive such dividend in cash or in property other than stock instead of stock) and whether distributed prior to, during, upon, or after liquidation or dissolution of the corporation:"

Section 47-1557a provides that "The words 'gross income' include * * * dividends * * * gains or profits, and income derived from any source whatever".

Section 47-1557b(11) provides that the words "gross income" shall not include "Gains from the sale or exchange of any capital asset as defined in this subchapter".

The facts, briefly stated, are the following:

The petitioners are former stockholders of Capitol. It was dissolved on January 29, 1960. At the time of its dissolution its financial condition, as reflected by its books and records was as follows:

Assets

Notes Receivable - Carlyle Realty Co.	$ 76,603.80
Accrued Interest on Carlyle Realty Co. note	3,937.50
Investment in Chastleton	
200 shares of preferred stock.	20,000.00
480 shares of common stock.	480.00
Total.	$101,021.30

Liabilities and Net Worth

Liabilities	None	
Common Stock, 500 shares	$ 1,200.00	
Earned Surplus.	99,821.30	$101,021.30

The stock in Chastleton was purchased by Capitol for the amount carried on its books, that is to say, for $20,480.00. No appreciation of value was realized by Capitol. The stock, along with other assets, was distributed to the stockholders on the day Capitol was dissolved, that is to say, on January 29, 1960, in proportion to their respective stockholdings. On February 1, 1960 the stockholders as a group sold the Chastleton stock for $390,000.00, which was distributed to the stockholders on the basis of their respective proportionate stockholdings.

The assessing authority of the District determined that all the petitioners received as dividends on the dissolution of Capitol were the assets following:

Notes and accrued interest: Carlyle Realty Co.	$80,541.30
Chastleton Hotel Enterprises, Inc. stock.	20,480.00
Total	$101,021.30

From that sum the assessing authority subtracted the amount of $1,200.00, representing the capital stock of Capitol, which was "paid-in

surplus" within the meaning of Section 47-1551c(m) of the Code, which made the total of the taxable liquidating dividends in the amount of $99,821.30. The assessing authority then proceeded on the premise, which the Court of Appeals held was correct, that the stockholders and not the corporation had sold the Chastleton stock. The amount which the stockholders received was $390,000. The assessing authority determined that the stockholders' basis for determining the total gain from the sale by the stockholders was $20,480.00; that they had held the stock for two days only; and computed the gain as follows:

Gain on sale of Chastleton Hotel Enterprises Stock

Selling Price	$390,000.00
Less Basis	20,480.00
Gain on Sale	$369,520.00

The assessing authority considered the foregoing liquidating dividend and the gain from the sale of the stock as received by each stockholder in the ratio or proportion as the dividends and proceeds of the sale of the stock were paid to the stockholders. An example of the computations is that determining the income tax liability of the petitioner, John H. Verkouteren, who owned 100 shares or 1/5 of the capital stock of Capitol, as follows:

Taxable income shown on return.		$ 23,573.57
Additional Income		
Dividend, Capitol, 1/5 x $99,821.30 (1)	$19,964.26	
Gain from sale of stock 1/5 x $369,520.00 (2)	73,904.00	93,868.26
Revised taxable income		$117,441.83
Revised tax liability.		$ 5,497.09
Less tax shown on return		810.81
Deficiency in tax.		$ 4,686.28

The determinations and computations of the assessing authority were proper, and the resulting assessments of the deficiencies here involved were valid.

The assessing authority correctly determined that the stockholders of Capital were not taxable on the unrealized appreciation of the value of Chastleton stock. District of Columbia v. Oppenheimer, 112 U.S. App. D.C. 239, 301 F.2d 563, 90 W.L.R. 559. It was equally correct in determining that the basis of the stockholders for determining gain from the sale by them of the Chastleton stock was not the unrealized, but the realized value, that is to say, $20,480.00. Oppenheimer v. District of Columbia, ____ U.S. App. D.C. ____, 363 F.2d 708, 94 W.L.R. 1281.

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(1) Total assets of Capitol, $101,021.30 distributed to its stockholders, less paid-in surplus of $1,200.00.

(2) Proceeds of sale of Chastleton stock $390,000, less the basis of $20,480.

For the reasons stated the Court holds as follows:

Docket No. 1897

That a deficiency in income tax for the calendar year, 1960, in the amount of $4,686.28, with interest in the amount of $609.22, or a total of $5,295.50, assessed against, and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

Docket No. 1898

That a deficiency in income tax for the calendar year, 1960, in the amount of $1,538.34, with interest in the amount of $199.98, or a total of $1,738.32, assessed against and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

Docket No. 1899

That a deficiency in income tax for the calendar year, 1960, in the amount of $1,497.01, with interest in the amount of $194.61, or a total of $1,691.62, assessed against and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

Docket No. 1900

That a deficiency in income tax for the calendar year, 1960, in the amount of $1,503.92, with interest in the amount of $195.51, or a total of $1,699.43, assessed against and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

Docket No. 1901

That a deficiency in income tax for the calendar year, 1960, in the amount of $3, 116.59, with interest in the amount of $405.16, or a total of $3,521.75, assessed against and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

Docket No. 1902

That a deficiency in income tax for the calendar year, 1960, in the amount of $1,564.47, with interest in the amount of $203.38, or a total of $1,767.85, assessed against and collected from the petitioners, is hereby affirmed; and that the petitioners are not entitled to any refund thereof.

Decision will be entered for respondent.

/s/ Jo V. Morgan
Judge

[Filed November 10, 1966]

John H. Verkouteren Docket No. 1897

DECISION ON REMAND

Upon consideration of the judgment of the United States Court of Appeals for the District of Columbia entered on May 11, 1965, and reversing the decision of this Court entered herein on March 4, 1964, and remanding this case; upon consideration of the petition filed herein; and upon the evidence adduced at the hearing on said petition, it is by the Court this 10th day of November, 1966,

ADJUDGED AND DETERMINED, That the decision of this Court entered herein on March 4, 1964, be and the same is hereby vacated and set aside,

AND IT IS FURTHER ADJUDGED AND DETERMINED, That a deficiency in income tax for the calendar year, 1960, in the amount of $4,686.28, with interest in the amount of $609.22, or a total of $5,295.50, assessed against, and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

* * *

/s/ Jo V. Morgan
Judge

[Filed November 10, 1966]

Herman Oshinsky Docket No. 1898

DECISION ON REMAND

Upon consideration of the judgment of the United States Court of Appeals for the District of Columbia entered on May 11, 1965, and reversing the decision of this Court entered herein on March 4, 1964, and remanding this case; upon consideration of the petition filed herein; and upon the evidence adduced at the hearing on said petition, it is by the Court this 10th day of November, 1966,

ADJUDGED AND DETERMINED, That the decision of this Court entered herein on March 4, 1964, be and the same is hereby vacated and set aside.

AND IT IS FURTHER ADJUDGED AND DETERMINED, That a deficiency in income tax for the calendar year, 1960, in the amount of $1,538.34, with interest in the amount of $199.98, or a total of $1,738.32, assessed against, and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

* * *

/s/ Jo V. Morgan
Judge

[Filed November 10, 1966]

Charles Oshinsky | Docket No. 1899

DECISION ON REMAND

Upon consideration of the judgment of the United States Court of Appeals for the District of Columbia entered on May 11, 1965, and reversing the decision of this Court entered herein on March 4, 1964, and remanding this case; upon consideration of the petition filed herein; and upon the evidence adduced at the hearing on said petition, it is by the Court this 10th day of November, 1966,

ADJUDGED AND DETERMINED, That the decision of this Court entered herein on March 4, 1964, be and the same is hereby vacated and set aside.

AND IT IS FURTHER ADJUDGED AND DETERMINED, That a deficiency in income tax for the calendar year, 1960, in the amount of $1,497.01, with interest in the amount of $194.61, or a total of $1,691.62, assessed against, and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

* * *

/s/ Jo V. Morgan
Judge

[Filed November 10, 1966]

William Oshinsky Docket No. 1900

DECISION ON REMAND

Upon consideration of the judgment of the United States Court of Appeals for the District of Columbia entered on May 11, 1965, and reversing the decision of this Court entered herein on March 4, 1964, and remanding this case; upon consideration of the petition filed herein; and upon the evidence adduced at the hearing on said petition, it is by the Court this 10th day of November, 1966.

ADJUDGED AND DETERMINED, That the decision of this Court entered herein on March 4, 1964, be and the same is hereby vacated and set aside.

AND IT IS FURTHER ADJUDGED AND DETERMINED, That a deficiency in income tax for the calendar year, 1960, in the amount of $1,503.92, with interest in the amount of $195.51, or a total of $1,699.43, assessed against, and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

* * *

/s/ Jo V. Morgan
Judge

[Filed November 10, 1966]

Herman Fenichel Docket No. 1901

DECISION ON REMAND

Upon consideration of the judgment of the United States Court of Appeals for the District of Columbia entered on May 11, 1965, and reversing the decision of this Court entered herein on March 4, 1964, and remanding this case; upon consideration of the petition filed herein; and upon the evidence adduced at the hearing on said petition, it is by the Court this 10th day of November, 1966,

ADJUDGED AND DETERMINED, That the decision of this Court entered herein on March 4, 1964, be and the same is hereby vacated and set aside.

AND IT IS FURTHER ADJUDGED AND DETERMINED, That a deficiency in income tax for the calendar year, 1960, in the amount of $3,116.59, with interest in the amount of $405.16, or a total of $3,521.75, assessed against, and collected from the petitioner, is hereby affirmed; and that the petitioner is not entitled to any refund thereof.

* * *

/s/ Jo V. Morgan
Judge

[Filed November 10, 1966]

Bernard Margolius and
Lilyan Margolius

Docket No. 1902

DECISION ON REMAND

Upon consideration of the judgment of the United States Court of Appeals for the District of Columbia entered on May 11, 1965, and reversing the decision of this Court entered herein on March 4, 1964, and remanding this case; upon consideration of the petition filed herein; and upon the evidence adduced at the hearing on said petition, it is by the Court this 10th day of November, 1966,

ADJUDGED AND DETERMINED, That the decision of this Court entered herein on March 4, 1964, be and the same is hereby vacated and set aside.

AND IT IS FURTHER ADJUDGED AND DETERMINED, That a deficiency in income tax for the calendar year, 1960, in the amount of $1, 564.47, with interest in the amount of $203.38, or a total of $1, 767.85, assessed against, and collected from the petitioners, are hereby affirmed; and that the petitioners are not entitled to any refund thereof.

* * *

/s/ Jo V. Morgan
Judge

[Filed November 16, 1966]

MOTION TO REVISE OPINION AND REQUEST FOR ORAL ARGUMENT

Pursuant to Rule 12(f) of the Rules of this Court, Petitioners, by their attorneys, Albert E. Arent and Joel N. Simon, respectfully move the Court to revise its Opinion (Opinion No. 1027-A, filed November 10, 1966) in the above cases to give consideration to the Petitioners' alternative argument that they are entitled to include in their holding period for the capital stock of Chastleton Hotel, Inc., the period of time in which such stock was held by Capitol Hotel Enterprises, Inc. Petitioners further move the Court to schedule oral argument on the "tacking" issue at a time convenient to the Court.

Petitioners, in their Brief, argued that in the event the Court should hold (as the Court did hold in its Opinion filed November 10, 1966) that petitioners are required to use as their basis for the capital stock of Chastleton Hotel, Inc., the basis of such stock in the hands of Capitol Hotel Enterprises, Inc., then petitioners were also entitled to include in their holding period such stock the period of time in which such stock was held by Capitol Hotel Enterprises, Inc. The Court, in its Opinion, did not discuss the issue of "tacking" of holding period, and the petitioners believe that oral argument on the "tacking" question would be of assistance to the Court in resolving this issue.

WHEREFORE, petitioners respectfully request that the within motion be granted.

/s/ Albert E. Arent

/s/ Joel N. Simon

[Filed February 7, 1967]

MEMORANDUM

The petitioners in the above entitled cases have filed a motion to revise the opinion of the Court and a request for oral argument. The motion was considered by the Court as a motion for reconsideration of the decisions of the Court. Oral argument on the question raised by the petitioners was had in deciding the case on remand. This Court in its original opinion overlooked the argument of the petitioners in their brief that in the event the Court should hold that the petitioners are required to use as their basis for the capital stock of Chastleton Hotel, Inc., the petitioners were entitled to adopt as their holding period for such stock the period of time which such stock was held by the Capitol Hotel Enterprises, Inc. The Court has considered the argument of the petitioners and has reconsidered its decisions in the case and does not believe it should change or in any way alter the decisions in the several cases. The Court did not hold in deciding these cases on remand that

the basis of the Capitol Hotel Enterprises, Inc. should be the basis of the stockholders. The question of capital gains or Capitol Hotel Enterprises, Inc. basis was not involved. All that was decided was that the basis of the stockholders in determining gain was the realized value of the asset they received from the corporation and then sold by them. The realized value happened to be the same as the basis of the Capitol Hotel Enterprises, Inc. but the case did not turn on that fact. The motion, considered as a motion for reconsideration will be denied. The period in which the petitioners may file a petition for review by the Court of Appeals begins upon the date of the denial.

/s/ Jo V. Morgan
Judge

[Filed February 2, 1967]

John H. Verkouteren Docket No. 1897

ORDER

Upon consideration of the motion of the petitioner to revise the opinion, which the Court has considered as a motion for reconsideration, it is by the Court this 2nd. day of February, 1967,

ORDERED, That the motion to revise the opinion considered as a motion for reconsideration be and the same is hereby denied.

/s/ Jo V. Morgan
Judge

WHEREFORE, petitioners respectfully request that the within motion be granted.

/s/ Albert E. Arent

/s/ Joel N. Simon

[Filed February 7, 1967]

MEMORANDUM

The petitioners in the above entitled cases have filed a motion to revise the opinion of the Court and a request for oral argument. The motion was considered by the Court as a motion for reconsideration of the decisions of the Court. Oral argument on the question raised by the petitioners was had in deciding the case on remand. This Court in its original opinion overlooked the argument of the petitioners in their brief that in the event the Court should hold that the petitioners are required to use as their basis for the capital stock of Chastleton Hotel, Inc., the petitioners were entitled to adopt as their holding period for such stock the period of time which such stock was held by the Capitol Hotel Enterprises, Inc. The Court has considered the argument of the petitioners and has reconsidered its decisions in the case and does not believe it should change or in any way alter the decisions in the several cases. The Court did not hold in deciding these cases on remand that

the basis of the Capitol Hotel Enterprises, Inc. should be the basis of the stockholders. The question of capital gains or Capitol Hotel Enterprises, Inc. basis was not involved. All that was decided was that the basis of the stockholders in determining gain was the realized value of the asset they received from the corporation and then sold by them. The realized value happened to be the same as the basis of the Capitol Hotel Enterprises, Inc. but the case did not turn on that fact. The motion, considered as a motion for reconsideration will be denied. The period in which the petitioners may file a petition for review by the Court of Appeals begins upon the date of the denial.

/s/ Jo V. Morgan
Judge

[Filed February 2, 1967]

John H. Verkouteren — Docket No. 1897

ORDER

Upon consideration of the motion of the petitioner to revise the opinion, which the Court has considered as a motion for reconsideration, it is by the Court this 2nd. day of February, 1967,

ORDERED, That the motion to revise the opinion considered as a motion for reconsideration be and the same is hereby denied.

/s/ Jo V. Morgan
Judge

[Filed February 2, 1967]

Herman Oshinsky Docket No. 1898

ORDER

Upon consideration of the motion of the petitioner to revise the opinion, which the Court has considered as a motion for reconsideration, it is by the Court this 2nd. day of February, 1967,

ORDERED, That the motion to revise the opinion considered as a motion for reconsideration be and the same is hereby denied.

/s/ Jo V. Morgan
Judge

[Filed February 2, 1967]

Estate of Charles Oshinsky Docket No. 1899

ORDER

Upon consideration of the motion of the petitioner to revise the opinion, which the Court has considered as a motion for reconsideration, it is by the Court this 2nd. day of February, 1967,

ORDERED, That the motion to revise the opinion considered as a motion for reconsideration be and the same is hereby denied.

/s/ Jo V. Morgan
Judge

[Filed February 2, 1967]

William Oshinsky — Docket No. 1900

ORDER

Upon consideration of the motion of the petitioner to revise the opinion, which the Court has considered as a motion for reconsideration, it is by the Court this 2nd. day of February, 1967,

ORDERED, That the motion to revise the opinion considered as a motion for reconsideration be and the same is hereby denied.

/s/ Jo V. Morgan
Judge

[Filed February 2, 1967]

Herman Fenichel — Docket No. 1901

ORDER

Upon consideration of the motion of the petitioner to revise the opinion, which the Court has considered as a motion for reconsideration, it is by the Court this 2nd. day of February, 1967,

ORDERED, That the motion to revise the opinion considered as a motion for reconsideration be and the same is hereby denied.

/s/ Jo V. Morgan
Judge

[Filed February 2, 1967]

Bernard Margolius and
Lilyan Margolius

Docket No. 1902

ORDER

Upon consideration of the motion of the petitioner to revise the opinion, which the Court has considered as a motion for reconsideration, it is by the Court this 2nd. day of February, 1967,

ORDERED, That the motion to revise the opinion considered as a motion for reconsideration be and the same is hereby denied.

/s/ Jo V. Morgan
Judge

[Filed February 28, 1967]

John H. Verkouteren

Docket No. 1897

PETITION FOR REVIEW OF A DECISION OF THE DISTRICT OF COLUMBIA TAX COURT

To the Honorable Chief Judge and the Circuit Judges of the United States Court of Appeals for the District of Columbia Circuit:

1. John H. Verkourteren petitions for a review by the United States Court of Appeals for the District of Columbia Circuit, of a decision of the District of Columbia Tax Court made in the above-entitled proceedings.

2. The decision of which review is sought affirmed an assessment of income tax for the calendar year 1960.

3. The Decision of the Tax Court was entered on November 10, 1966. On November 16, 1966, the Petitioner filed a Motion for Reconsideration of the Decision of the Tax Court. This Motion was denied by the Tax Court on February 2, 1967.

/s/ Albert E. Arent

/s/ Joel N. Simon

Attorneys for Petitioner
1000 Federal Bar Building
1815 H Street, N. W.
Washington, D. C. 20006

[Identical Petitions for Review were filed in the Tax Court in the other consolidated cases, Docket Nos. 1898 - 1902, on February 28, 1967]

En Banc
6-19-69
(20)

BRIEF FOR RESPONDENT

IN THE
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 20,889 - 20,894

JOHN H. VERKOUTEREN, ET AL.,

Petitioners,

v.

DISTRICT OF COLUMBIA,

Respondent.

ON PETITION FOR REVIEW OF DECISIONS
OF THE DISTRICT OF COLUMBIA TAX COURT

CHARLES T. DUNCAN
Corporation Counsel, D. C.
HUBERT B. PAIR
Principal Assistant Corporation
Counsel, D. C.
HENRY E. WIXON
Assistant Corporation Counsel, D. C.
ROBERT C. FINDLAY
Assistant Corporation Counsel, D. C.

Attorneys for Respondent
District Building
Washington, D. C. 20004

QUESTIONS PRESENTED

Where, in the stipulation of the parties, it is stated that Capitol Hotel Enterprises, Inc. was dissolved on January 29, 1960, and that its shareholders received upon its dissolution their proportionate share of its assets, including preferred and common stock of Chastleton Hotel, Inc.; and where, only three days later on February 1, 1960, the shareholders sold their Chastleton stock to a single purchaser for $390,000, in respondent's view, the questions presented are:

1. Is not the basis of the Chastleton stock, for the calculation of petitioners' gain or loss upon its sale after dissolution of Capitol, the amount of the liquidating dividend represented in that stock?

2. Because neither the District of Columbia Income and Franchise Tax Act of 1947, nor any regulation promulgated thereunder, authorizes it, is it not correct that petitioners are not entitled to add to the three-day period during which they held Chastleton's stock, either the period during which Capitol held that stock or the period during which petitioners held Capitol's stock?

3. Should not book values, rather than fair market values, be employed as the basis for the allocation of "earnings, profits, or surplus" among the assets distributed to petitioners?

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TABLE OF CASES

* Cases principally relied upon

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STATUTES CITED

OTHER AUTHORITY CITED

IN THE
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

JOHN H. VERKOUTEREN, ET AL.,

Petitioners,

v.

DISTRICT OF COLUMBIA,

Respondent.

Nos. 20,889 - 20,894

BRIEF FOR RESPONDENT

COUNTER-STATEMENT OF THE CASE

Capitol Hotel Enterprises, Inc. (hereafter referred to as "Capitol") was organized in 1948 as a Delaware corporation. That same year, Capitol purchased, for $20,000, 200 shares of the preferred stock and, for $480, 480 shares of the common stock of Chastleton Hotel, Inc. (hereafter referred to as the "Chastleton stock"). On January 29, 1960, Capitol was dissolved. Upon dissolution, each petitioner received in complete cancellation and redemption of the common stock of Capitol stock owned by him, his proportionate interest in the assets of the corporation, including the Chastleton stock.[1] Three days later, on

---

1. Petitioners-shareholders received 120 shares of the 200 shares of preferred stock distributed and 288 shares of the 480 shares of common stock distributed.

February 1, 1960, each petitioner sold the Chastleton stock so received by him "to a single purchaser for a total purchase price for all such shares of Chastleton stock of $390,000." (J.A. 11-15.)

Thereafter, the District assessed deficiencies in income tax for the year 1960 against each petitioner with respect to his pro rata share of the dividend from Capitol and the gain on the sale of the Chastleton stock. Petitioners appealed from the assessments of deficiencies to the District of Columbia Tax Court which, on March 4, 1964, affirmed such assessments. On appeal, this Court, in Verkouteren v. District of Columbia, 120 U.S.App.D.C. 361, 346 F.2d 842 (1965), reversed the decisions of the Tax Court and remanded the cases to that court for further proceedings. Upon remand, the Tax Court accepted and found the facts as stipulated by the parties (J.A. 17), and again affirmed the assessments against petitioners, concluding that:

> "The assessing authority correctly determined that the stockholders of Capitol were not taxable on the unrealized appreciation of the value of Chastleton stock. District of Columbia v. Oppenheimer, 112 U.S. App.D.C. 239, 301 F.2d 563, 90 W.L.R. 559. It was equally correct in determining that the basis of the stockholders for determining gain from the sale by them of the Chastleton stock was not the unrealized, but the realized value, that is to say, $20,480.00. Oppenheimer v. District of Columbia, _____ U.S.App. D.C. _____, 363 F.2d 708, 94 W.L.R. 1281." (J.A. 21.)

It is from these decisions of the Tax Court that petitioners, on February 28, 1967, appealed to this Court. (J.A. 35-36.)

SUMMARY OF ARGUMENT

Upon dissolution of Capitol on January 29, 1960, its shareholders received a pro-rata share of the assets of that corporation, including preferred and common stock of Chastleton Hotel, Inc. Three days thereafter, on February 1, 1960, the former shareholders of Capitol sold their Chastleton stock to a single purchaser for $390,000.

The basis for gain or loss on the sale of the Chastleton stock in the shareholders' hands was $20,480, which figure represents the earned surplus of Capitol attributable to that stock on the date of Capitol's dissolution. Since petitioners, as a group, owned 300 shares out of 500 shares of Capitol's outstanding common stock, the total earned surplus attributable to them was three-fifths of $20,480, or $12,288. This amount was taxed as a dividend to the petitioners.[2] When a corporation is dissolved and distributes its assets in kind, the basis for gain or loss on a later sale or exchange of these same assets is the amount of the dividend represented in the value of the assets received.

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2. Without regard to the de minimis amount of capital investment included in the book value of the stock, which has not been an issue in this case.

Petitioners are not authorized, under the alternative theories advanced by them, to employ the process of "tacking" to determine their holding period of the Chastleton stock in order that they may receive capital gains treatment by virtue of being considered to have "owned" such stock for more than two years. Neither the District of Columbia statute, nor any regulation promulgated thereunder, authorizes it. Congress, despite ample opportunity, has not yet enacted statutory authority therefor, and this inaction is indicative of its intention not to do so.

The basis of allocation among the assets distributed to petitioners of the total dollar amount of the distributions, as reflected on Capitol's records, must be book, rather than fair market, values, because to compute the basis otherwise would result in distortion of the earnings, profits, and surplus represented by the assets actually received by petitioners.

ARGUMENT

I.

The basis of the Chastleton stock, for calculation of petitioners' gain or loss upon its sale after dissolution of Capitol, is the amount of the liquidating dividend represented in such Chastleton stock.

Under the District of Columbia Income and Franchise Tax Act of 1947, amounts distributed by a corporation to shareholders in complete

liquidation of the corporation, which amounts represent the earnings, profits, or surplus earned by it, are treated as dividends. District of Columbia v. Oppenheimer, 112 U.S.App.D.C. 239, 301 F.2d 563 (1962); Berliner v. District of Columbia, 103 U.S.App.D.C. 351, 258 F.2d 651, cert. denied, 357 U.S. 937 (1958). Unrealized appreciation in the value of property distributed upon corporate liquidation is not taxable as a dividend except to the extent that that appreciation is represented by a distribution of earnings, profits, or surplus of the distributing corporation. District of Columbia v. Oppenheimer, supra. Consequently, when a corporation is dissolved and distributes its assets in kind, the basis for gain or loss on a later sale or exchange of the same assets is the amount of the liquidating "dividend" represented in the value of the assets received. In the instant case, the basis of the assets distributed upon dissolution of Capitol was $99,821.30, which was the earned surplus of Capitol on the date of dissolution and therefore the amount which was taxable as a "dividend" distribution to its shareholders.

The Tax Court discussed the basis of assets received upon a corporate dissolution in the second Oppenheimer case, Oppenheimer v. District of Columbia, Opinion No. 1029 (April 9, 1964), aff'd, 124 U.S. App.D.C. 221, 363 F.2d 708 (1966), which involved the proper basis to be used for depreciation purposes. There the Tax Court said:

"Several sections of the District of Columbia Income and Franchise Tax Act of 1947, as codified in the Code, should be examined and discussed. (1) The first is Section 47-1551c(m) defining a dividend. It is as follows:

'The word "dividend" means any distribution made by a corporation (domestic or foreign) to its stockholders or members, out of its earnings, profits, or surplus (other than paid-in surplus) whenever earned by the corporation and whether made in cash or any other property (other than stock of the same class in the corporation if the recipient of such stock dividend has neither received nor exercised an option to receive such dividend in cash or in property other than stock instead of stock) and whether distributed prior to, during, upon or after liquidation or dissolution of the corporation: Provided, however, That in case of any dividend which is distributed other than in cash or stock in the same class in the corporation and not exempted from tax under this subchapter, the basis of tax to the recipient thereof shall be the market value of such property at the time of such distribution; * * *.' (Emphasis supplied.)"

"The next section of the Code to be considered is Section 47-1583c. It is found in Title XI of the Income and Franchise Tax Act, entitled 'Bases', and reads as follows:

"(1) A 'dividend' is taxable under Section 47-1557a(a), D.C. Code, 1961 Edition."

'Bases for dividends paid in property.[(2)] Where any property other than money is paid by a corporation as a dividend, the base to the recipient thereof shall be the market value of such property at the time of its distribution by such corporation.' (Emphasis supplied.)"

"Before citing and discussing the third and last pertinent provision in the Code [not applicable to this case], it should be noted that the provision in Section 47-1551c(m) that the bases of tax shall be 'the market value', and that in Section 47-1583c that the 'base' (for all purposes) shall be 'the market value' apply solely to those cases or instances wherein the property involved is distributed as a dividend. Such provision in Section 47-1551c(m) does not apply where the property distributed is not a dividend and not taxable as such. District of Columbia v. Oppenheimer, 112 U.S. App. D.C. 239, 301 F.2d 563, 90 W.L.R. 559. The same is true in respect to the same provision in Section 47-1583c. Expressio unius, exclusio alterius. If Congress had intended that the basis for property distributed by a corporation otherwise than a dividend should be 'the market value', it could have eliminated the phrase 'as a dividend', so that the phrase would have read 'where any property other than money is paid by a corporation'." (Brackets added.) (pp. 9-10.)

In affirming on appeal, this Court agreed, saying that to allow petitioners to utilize a basis representing fair market value would mean

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"(2) Since the provision is without limitation, the basis is for both the determination of capital gain or loss and for depreciation purposes."

> " * * * that a stockholder, simply by deciding to dissolve and liquidate the corporation, may acquire a depreciation base consisting of a book write-up of a value on which, very properly, no tax need be paid upon its receipt by the stockholder. We think it much more likely that Congress intended to have its express—and only—language in the District taxing statute on corporate distributions in liquidation point the way for handling depreciation basis of property distributed in liquidation." (124 U.S.App. D.C. 221, 224, 363 F.2d 708, 711 (1965).)

Oppenheimer thus presented a contention analogous to that advanced by petitioners here, viz., that the properties received by Mrs. Oppenheimer upon dissolution of the corporation in which she had owned stock were to be valued thereafter while in her hands at their fair market value at the time they were distributed to her in liquidation. As indicated above, although the question there raised concerned the depreciation basis of the properties owned by her, it is clear that her contention would have been the same had she sold the properties. And the case of Dupont Park Apartments, Inc. v. District of Columbia, 120 U.S.App.D.C. 215, 345 F.2d 109 (1965), referred to by Judge Danaher in his statement of separate views in Oppenheimer, is a case which lends further authority for the rejection of petitioners' premise that they are entitled to what amounts to a "stepped-up" basis in the value of the assets disposed of by them following the dissolution of Capitol.

In discussing the concept of basis and its applicability under the Internal Revenue Code, Mertens, Law of Federal Income Taxation, Vol. 3A, section 21.01 states as follows:

> "The key which unlocks the door to understanding here is the general rule that both the taxpayer and the Commissioner are to be kept whole no matter how many transactions and permutations occur. Gain is in the end to be completely taxed once, but only once. Conversely, loss in the end is to be completely deducted (apart from artificial statutory limitations) once, but not more than once. Any system of taxation worthy of the name must at least strive to do that. And where in rare instances it has not done so, it will be found that Congress thought there were countervailing considerations which justified the abandonment of the rule. Likewise, a number of the statutory provisions are intended to present a stepped-up basis without collection of tax on the increase in value." (Footnote omitted.)

Here, both the taxpayer and the government will be kept whole where the basis is determined to be the amount of the dividend received by the shareholders and represented in the value of the assets received. The amount of this dividend, equal to the earned surplus of Capitol on the date of dissolution, was $99,821.30.

Petitioners' argument that the value of the assets held by Capitol was $470,541.30 (Brief for Petitioners, p. 15), rather than their book value, and that the increased value was the value of petitioners' common stock in Capitol surrendered by them upon dissolution, is substantially identical to the contention of the District in the "first

Oppenheimer case," an argument rejected by both the Tax Court and by this Court. District of Columbia v. Oppenheimer, 112 U.S. App.D.C. 239, 301 F.2d 563 (1962). Moreover, that case, unlike this one, involved the question of the amount of a "dividend" which would be subject to tax upon its receipt by Mrs. Oppenheimer.

Petitioners also urge that they received in distribution upon liquidation of Capitol only an amount equivalent to the value of the shares of that corporation's stock which each of them surrendered, and that the portion of the liquidating distribution in excess of the corporation's earned surplus was received in exchange for the underlying stock (Brief for Petitioners, pp. 6-9). This contention is comparable to that advanced by the taxpayers in Berliner v. District of Columbia, supra, which the Court rejected on the ground that a liquidating distribution is not, under the District statute, to be treated as a sale or exchange of stock. There the Court was emphatic in pointing out that, whereas federal income tax law currently contains a specific provision that amounts distributed in complete corporate liquidation shall be treated as in full payment in exchange for the stock, the District statute, also congressionally enacted, contains no similar provision. Moreover, the Court said, District law defines "dividend" in virtually the same way as federal statutes have since 1916, and also contains a specific provision that a "dividend" includes a

distribution of earnings "during, upon, or after liquidation." D.C. Code, § 47-1551c(m), supra at 6. As this Court succinctly stated:

> " * * * Had Congress intended that such a distribution be treated as an exchange, we think it would have omitted the reference to liquidating distributions in the definition of a dividend and would have included a provision similar to that which has appeared in the Federal statutes uninterruptedly since 1924. * * *
>
> " * * * If distributions like the present were treated as sales or exchanges of stock, * * * some stockholders (those who had owned their stock for more than two years) would escape tax altogether on receipt of the corporate earnings whereas other stockholders would be taxed in full on receipt of exactly the same distribution of earnings merely because they had held their stock for only two years or less. Such a difference in treatment for the same distribution would hardly be justified by logic—and, as we read the statutes, Congress has not authorized it. * * *" (103 U.S.App.D.C. 351, 354-55, 258 F.2d 651, 654-55 (1958).)

From this it is abundantly evident that a transaction like the one in these cases is, contrary to petitioners' contention, not a "sale or exchange" of stock.

Additionally, petitioners rely heavily upon this Court's decision in Snow v. District of Columbia, 124 U.S.App.D.C. 69, 361 F.2d 523 (1965), which they contend supports their position as to the effect upon them of the liquidating distribution by Capitol. However, Snow involved a matter entirely different from that here in issue. There the Court dealt

with the question whether Snow, who in order to acquire an apartment house owned by a corporation had purchased all its stock and immediately thereafter liquidated such corporation, was liable for income tax upon the amount of the corporation's earned surplus distributed to him. It was held that Snow was liable, but that he had sustained a non-capital, and therefore a fully deductible, loss to the extent of the earned surplus when "in the other part of the transaction he received $700,000 of assets in return for the surrender of stock for which he paid $1,000,000 in cash." (124 U.S.App.D.C. 69, 73, 361 F.2d 523, 527 (1965).)

Snow, therefore, is in no sense comparable to the situation here presented. These cases do not relate to the taxability of the dividend, on the one hand, and the resultant loss on the other, but concern rather the question of the taxability of petitioners with respect to a gain realized by them upon a subsequent sale of assets received by them in liquidation.

It is therefore submitted that the Berliner and second Oppenheimer cases, supra, are controlling as to both the concepts of exchange and of stepped-up basis for the assets here involved, and that those decisions should be followed by this Court.

II.

Petitioners are not entitled to add to the three-day period during which they held Chastleton's stock, either the period during which Capitol held that stock or the period during which petitioners held Capitol's stock, because neither the District of Columbia Income and Franchise Tax Act of 1947, nor any regulation promulgated thereunder, authorizes it.

Title III, section 2(b)(B)(11) of the District of Columbia Income and Franchise Tax Act of 1947 (D.C. Code, 1961, § 47-1557a(b)(11)) states that gross income shall not include "gains from the sale or exchange of any capital assets * * *." Title I, section 4(l) of the Income and Franchise Tax Act (D.C. Code, 1961, § 47-1551c(l)) defines a capital asset as follows:

> "The words 'capital assets' mean any property, whether real or personal, tangible or intangible, held by the taxpayer for more than two years (whether or not connected with his trade or business), but do not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the end of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

Petitioners contend that they are entitled to capital asset treatment in this transaction since, by derivation from Capitol, they are to be considered as having "owned" the Chastleton stock for more than two years. Significantly, petitioners at the same time recognize that, while federal income tax law contains a specific provision on this matter, the

District's statute does not. Indeed, it is this fact that is crucial with respect to petitioners' argument on this point.

Petitioners refer to section 1223(2) of the Internal Revenue Code of 1954, and urge that it, by analogy, is applicable here. That section provides:

> "In determining the period for which the taxpayer has held property however acquired there shall be included the period for which such property was held by any other person, if under this chapter such property has, for the purpose of determining gain or loss from a *sale or exchange*, the same basis in whole or in part in his hands as it would have in the hands of such other person." (Emphasis added.)

In effect, section 1223(2) states that where the transferee of property is *required* to use the transferor's basis, then the period during which the transferor held the property is included in computing the period during which the transferee holds it. In these cases, however, the basis is not required to be determined by reference to the transferor~~'s basis~~, but is, instead, determined by reference to the earned surplus of the corporation distributed upon its dissolution. Petitioners' argument concerning this section is of necessity dependent upon specific federal treatment of such a transaction as this as a "sale or exchange." But, as shown in Part I of this brief, this transaction is, under District law, simply not a "sale or exchange." *Berliner* v. *District of Columbia*, *supra*.

Moreover, the Internal Revenue Code of 1954 contains a number of provisions related entirely to corporate liquidation, basis for assets, and the recognition of gain or loss upon the receipt by a stockholder of the assets of a completely or partially liquidated corporation. See, e.g., I.R.C. secs. 331 et seq. No provisions comparable to these are contained in the District's statute. Therefore, section 1223(2), even if it could be applied by analogy, is inapplicable to the facts of the instant cases.

But beyond this, the fact remains that there is no statutory provision whatsoever in the District of Columbia Income and Franchise Tax Act which authorizes the "tacking" process which petitioners seek to have this Court permit; nor is there any regulation so permitting. Congress, which a number of years ago enacted the allegedly analogous section quoted above, has had ample opportunity over those years to change the District law, but has not done so. "Expressio unius, exclusio alterius." Furthermore, the very simple fact that Congress has chosen to establish widely varying holding periods to mark the line between capital and non-capital transactions under District and federal law (two years vs. six months) clearly shows that it intended different treatments on this subject.

Petitioners cite District of Columbia v. Lewis, 109 U.S. App. D.C. 353, 288 F.2d 137 (1961) in support of their argument in favor of

a tacking of holding period, saying that that decision held that the rules and interpretations of federal statutes should be applied to cognate provisions of the District's Income and Franchise Tax Act. Petitioners also say that the Court in Lewis " * * * went so far as to require that language contained in a Federal statute, not found in a cognate provision of the District of Columbia Income Tax Act, be written into the latter as if it had originally appeared therein." (Brief for Petitioners, p. 35.) This Court there did not so hold. Rather, Lewis involved the first-time interpretation of a phrase in a District taxing statute which was identical to that contained in the Internal Revenue Code on the same subject. Under these circumstances, this Court ruled only that interpretation "guidance" could be obtained from decisions under the federal statute construing the phrase. Here, however, there is presented an entirely different situation, because here there is no statutory provision in the District law than can be compared with a like provision in the federal law. Hence, the holding in Lewis is inapplicable.

And, the words of this Court in Eastman Kodak Co. v. District of Columbia, 76 U.S.App.D.C. 339, 131 F.2d 347 (1942) are significant on this point, wherein it was said:

> "* * * Petitioner relies * * * upon the provision in the District of Columbia Revenue Act of 1939, Sec. 29(a) [which, it is to be noted, does not appear in the District's 1947 Income and Franchise Tax Act], that the assessor 'shall apply as far as practicable the administrative and judicial interpretations of the Federal income tax law so that computations of income for purposes of this title * * * shall be, as nearly as practicable, identical with the calculations required for Federal income tax purposes.' But the language just quoted can apply only to those parts of the Federal law which are like parts of the District of Columbia law. There is nothing in the District law which even remotely resembles the * * * language of [the federal provision sought to be compared]. * * *" (76 U.S.App. D.C. 339, 341, 131 F.2d 347, 349 (1942); brackets added; footnote omitted.)

Moreover, to accept petitioners' position under Lewis would result in a complete escape by petitioners from District tax when, under federal law, no such result would be forthcoming, since the effect of tacking is merely to change the rate of tax applicable to a subsequent transaction. In other words, the application of Lewis in the manner petitioners suggest here would bring about only greater disharmony, rather than harmony.

The assets involved in the instant case were held by these petitioners for a period of but three days, i.e., from January 29 to February 1, 1960, before they were disposed of by them through sale. These assets were not capital assets in petitioners' hands, regardless of what they might have been when owned by Capitol, and the gain realized

by petitioners upon the sale was therefore fully taxable. Any other result would permit petitioners to escape the tax which this Court in Berliner, supra, so aptly pointed out would hardly be the intent of Congress. In this connection, the comments of the Court in that case, quoted supra at p. 11, are equally appropriate here, since petitioners, upon the premises which they advance, would escape taxation entirely. Thus, the incident of time rejected in Berliner is likewise subject to rejection here.

Petitioners cite Helvering v. New York Trust Company, 292 U.S. 455 (1934) as authority for the proposition that the tacking principle should be allowed here, despite the fact that, as aforementioned, District law does not accord that principle explicit statutory recognition. Helvering dealt with a transfer to a trust established for the benefit of a son of corporate stock which his father had held for more than two years. Subsequently, the trust, before it itself held the stock for two years, sold it. There is nothing in that decision to indicate that the same rule there laid down with respect to trusts applies to stockholders or to corporate liquidations such as is the situation here. And particularly is this true when federal income tax law contains specific provisions on the subject of tacking.

In view of the foregoing, it is submitted that the stock sold by petitioners was held by them for a period of less than two years after

its receipt. Since District statutory provisions pertaining to capital assets provide that a taxpayer must hold property for more than two years before it can constitute a capital asset, and thereby be given favored treatment, the gain from this sale is includible in the gross income of petitioners.

III.

Book values, rather than fair market values, should be the basis for allocation of "earnings, profits or surplus" among the assets distributed to petitioners.

Petitioners contend, alternatively, "* * * that in any event they are entitled to use as the basis for the Chastleton Stock distributed to them an amount equal to that portion of Capitol's earned surplus which the fair market value of the Chastleton Stock bore to the fair market value of all assets distributed by Capitol on liquidation." (Brief for Petitioners, p. 41.)

It was stipulated by the parties and found by the Tax Court that the earned surplus of Capitol at the time of dissolution was $99,821.30; that the capital investment in Capitol was $1,200; and that the sum of these two amounts was represented solely by intangible assets having a total book value of $101,021.30. Two of these assets, viz., notes receivable in the amount of $76,603.80, and accrued interest receivable

in the amount of $3,937.50, were stipulated to have values equal to those shown on the balance sheet of the corporation as of January 29, 1960, immediately prior to their distribution to the stockholders (J.A. 14, 16). Only the remaining assets of Capitol, i.e., the Chastleton Hotel stock with a book value of $20,480, had a greater actual fair market value, $390,000 (J.A. 14, 16). Thus, all of the assets distributed to petitioners had actual values at least equal to or in excess of the earnings, profits, and surplus of Capitol at the time of its dissolution. Inasmuch as the capital investment of the stockholders amounted to only $1,200, the balance of the values of the assets exactly equaled the distributed earnings, profits, and surplus.

The second Oppenheimer case, supra, established that where an asset in kind is distributed to a stockholder, only the amount of earnings, profits, and surplus represented in the fair market value of that asset may be subjected to tax by the District as a dividend, irrespective of the fact that the fair market value of such asset exceeds the earnings, profits, and surplus so distributed. Petitioners' contention that they are entitled to attribute to the Chastleton Hotel stock a basis greater than that represented by earnings, profits, and surplus, applicable to that stock as reflected on the books of the corporation would, if accepted, result in distortion of the earnings, profits, and surplus represented by

the assets actually received by the stockholders. Under petitioners' contention, the earned surplus represented in notes receivable would not be \$76,603.80, the actual value thereof as shown on the balance sheet of the corporation, but would be only \$16,250; and the earned surplus represented by accrued interest receivable would not be \$3,937.50 as shown on the books, but would be only \$837.00. Under such manipulation, the earned surplus pertinent to the Chastleton Hotel stock, stated on the books to be \$20,480.00, would be increased to \$82,900.[3]

Disregarding the *de minimis* amount of capital investment, the total value of the assets distributed equals the earnings, profits, and surplus of Capitol at its dissolution, and the basis of these assets in the hands of the stockholders is the amount of the dividend which they represent, unaffected by market value.

CONCLUSION

It is respectfully submitted that the affirmance by the District of Columbia Tax Court of the assessments of income tax involved was correct and should be sustained.

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3. All computations are to slide rule accuracy.